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THE EXCESS PROFITS TAX ACT

W. D. TAMBLYN

A Chartered Accountant discusses the Excess Profits Tax Act, dispelling some popular misconceptions concerning it and commenting upon specific sections of the Act, such as those dealing with "Standard Period," "Standard Profits" and "Inventory Reserve."

* * *

Appropriateness of the Name "Excess Profits Tax Act"

THE name "Excess Profits Tax" is somewhat misleading, for all concerns not specifically exempted are subject to a minimum tax under the Act of 12% of net taxable profits, regardless of the relation of profits earned to any standard. Furthermore, the name suggests a tax applicable to profits above an allowed return, of which the normal measure would be a percentage return on capital invested. Such allowed return, however, is in ordinary cases not determined by the Act but by the past experience of the taxpayer. Thus, a taxpayer who during the period 1936 to 1939 has earned 100% on capital is subject only to the minimum tax of 12%, provided his rate of earnings does not substantially increase.*

25% of profits that represented a return of 10% - 15% of capital.*
50% of profits that represented a return of 15% - 20% of capital.
75% of profits that represented a return on capital in excess of 20%.

***Under the Act the excess profits tax is the greater of 12% of the net taxable profit or 75% of (the excess profit less 18% income tax). In practice the 75% rate is, therefore, not applied unless the profit in the chargeable period exceeds the standard profit by more than 24.24% of such standard profit.**

***Roughly speaking, capital was taken to be the amount of paid-up capital stock plus surplus and free reserves.**

The Act, then, apart from the 12% minimum tax, which in reality amounts to an increase in the rate of income tax, might more appropriately be termed a war profits tax.

Popular Misconceptions Concerning the Act

It appears to be the popular belief, in accordance with Colonel Ralston's statement in his budget speech, that the present taxation provisions are the most drastic which have ever been imposed on this country. In general this statement cannot, of course, be challenged but in comparison we should not overlook the predecessor of the present Excess Profits Tax Act, passed in 1916, and known as the Business Profits War Tax Act. The rates imposed by this Act were quite severe even in the light of present standards. These tax rates, as amended in 1917 and applying to limited companies with a capital in excess of $50,000.00, were as follows:

It is evident from an examination of the above figures that even with the addition of income tax concerns earning a consistently high return on capital would be more leniently treated under the present Act than under the Business Profits War Tax Act.

A further popular belief, reflected in an amendment proposed at the last session of parliament to increase the excess profits tax rate from 75% to 100%, is that the English Excess Profits Tax Act, imposing as it does a 100% rate, is more severe than the Canadian Act. It was pointed out, however, by those opposed to the amendment that in England there is no tax corresponding to our corporation income tax. Thus, English companies not earning excess profits pay no income or excess profits tax, whereas Canadian companies are taxed a minimum of 30% federal tax and rates up to 10% by provincial governments. In Ontario taxes on excess profits would be as follows:

Income tax	18%
Excess profits tax, 75% of 82%	61.5%
Ontario corporation income tax	5%
	84.5%

Comments Upon Specific Sections in the Act

Certain sections in the Act, over which there has been considerable controversy, both as to interpretation and equity afforded the various classes of taxpayers, are commented upon as follows:

Standard Period:

Section 2(h) "'standard period' means the period comprising the calendar years one thousand nine hundred and thirty-six to one thousand nine hundred and thirty-nine, both inclusive, or the fiscal periods of the taxpayer ending in such calendar years or those of such years or fiscal periods since January first, one thousand nine hundred and thirty-six, during which the taxpayer was carrying on business."

In an explanatory brochure recently published under the names of the Minister of National Revenue and Commissioner of Income Tax, this section is interpreted as describing a factual condition. The interpretation is that the standard period of firms with fiscal years coinciding with calendar years will be the calendar years 1936 to 1939 inclusive, but if fiscal years do not coincide with calendar years the standard period is then comprised of the fiscal years ending in the calendar years 1936 to 1939.

The effect of this section of the Act, then, is that, except in the case of firms whose accounts are made up on a calendar year basis, a portion of the profits earned in the calendar year 1939 will be left out of the calculation of standard profits and a corresponding portion of 1935 results substituted. As business conditions were generally much better in 1939 than in 1935, this means that firms with a year end prior to 31st December will be penalized and, broadly speaking, the earlier the year end the greater the discrimination.

There would seem to be no adequate reason from an administrative standpoint for the computation of standard profits on a fiscal rather than on a calendar year basis. Whereas it would be impracticable for a business, which ended its year at other than the 31st of December, to arrive at actual net taxable profits for calendar years, a reasonably accurate result should be obtained by allocating profits on a monthly or per diem basis. The principle of the per diem allocation of profits has already been accepted under the Act in the allotment of profits to the year 1940 and in explaining this treatment of profits, Colonel J. L. Ralston, in his budget speech, made the following statement, "In order that firms may not receive discriminatory treatment because their fiscal years happen to end on different dates, it will be recommended that the tax in respect of all businesses shall apply to profits earned on and after the same date, namely January 1st, 1940, regardless of the expiry date of the fiscal year." Had this concession not been made, however, and had firms, as a result, been taxed on a full year's profits for the fiscal

year ended in 1940, they would undoubtedly have received compensating relief in the year the tax was lifted, as was the case under the Business Profits War Tax Act.

It is contended, therefore, that by not allowing the standard period to be reckoned on a calendar year basis or even by not making such basis mandatory a more serious discrimination has resulted than is corrected by Section 16 to which Colonel Ralston referred.

The Act has been criticized for the selection of the four-year period 1936 to 1939 as unfair to certain industries that have emerged more slowly than others from the depression *(e.g.,* the so-called heavy or construction industries). In fact, the committee on federal taxation of the Institute of American Accountants gave recognition to the fact by suggesting optional periods for the computation of standard profits, 1924 to 1927 or 1936 to 1939. Such a suggestion does not seem altogether practical because of complications arising by reason of capital and other changes, but at any rate the inequity of not allowing profits to be averaged on a calendar year basis is emphasized in the case of such industries. A certain measure of relief is, of course, promised in the section of the Act dealing with depressed industries.

Standard Profits:

2(i) " 'standard profits' means the average yearly profits derived by a taxpayer in the standard period from carrying on the same general class of business as the business producing the profits in the year of taxation, or the standard profits as determined in accordance with section five of this Act. Provided, however, that losses incurred by the taxpayer during the standard period shall not be deducted from the profits in the standard period but the years or fiscal periods when such losses were incurred shall nevertheless be counted in determining the average yearly profits during the said standard period."

While in the majority of cases the standard profits will be calculated from the results of four fiscal periods of twelve months each, it is possible that a business may have ended more or less than four fiscal periods in the calendar years 1936 to 1939, or that the number of months in the standard period will not in the aggregate amount to forty-eight. The standard profit must then be arrived at by taking a twelve-month arithmetical average.

Adjustment of Standard Profits:

4(l) "The Minister may in his discretion make the following adjustments in the standard profits of a taxpayer:

(a) "adjust the standard profits to the basis of a fiscal period or fraction thereof comparable in length with the fiscal period or fraction thereof of the year of taxation."

No adjustment of standard profit is called for under this section unless the taxation period is not a twelve-month period. If such is the case, the adjustment of standard profit is calculated by using a monthly average.

(b) "adjust the standard profits, by reference to any increase or decrease in capital contributed or withdrawn to such a basis that the capital employed during the standard period is comparable with the capital employed during the taxation period."

The interpretation of this section according to the Minister's explanatory brochure is that "by reference to" means "only in those cases where there has been" and further that "by 'contributed' is meant furnished from outside the business as for instance in the case of a company, from the shareholders. Thus, in the case of a company, accumulated earnings are not 'contributed' capital; but new capital from the shareholders in exchange for shares is 'contributed' capital. Before undistributed profits of a company can rank as 'contributed' capital they must be capitalized by means of a stock dividend, for instance, or by being paid out as a cash dividend and then being used by the shareholders to subscribe for new stock in the company." The brochure further states that capital for all purposes is computed in accordance with the First Schedule of the Act.*

It is clear that it is not the Minister's intention to allow a company any adjustment of standard profits in respect of capital increased solely by means of accumulated profits. Furthermore, it is presumed that the Minister will use his discretionary power to exclude from benefit under this section any business not the recipient of a substantial "contribution" to capital. Where an adjustment of standard profits is allowed, however, the addition to net assets resulting from earnings as well as from capital "contributed" must, in accordance with the definition of capital employed in the Act, be included in the capital employed

*Capital is defined under the First Schedule of the Act roughly as the cost value of assets purchased plus a reasonable value for assets otherwise acquired, exclusive of investments producing tax exempt income and unproductive assets, less government subsidies, depreciation, depletion, debts, other than dividends declared but unpaid, and borrowed money. Provision is made only for the computation of capital employed in any year or fiscal period and is taken as capital at the beginning of the said period. In the taxation period beginning capital is further adjusted pro rata for additions to or reductions of assets, other than additions or reductions resulting from profits and losses, and by a deduction of one-half the amount of dividends paid during such period.

at the beginning of both taxation period and fiscal years in the standard period. Thus, a company obtaining an adjustment of standard profits under this section of the Act would appear to receive full benefit in respect of its increased capital without regard to the source of such increase.

The adjustment of standard profits according to the Minister's brochure is made as follows:

$$\frac{\text{Capital Employed in the Taxation Period} \times \text{Standard Profit}}{\textit{Average capital employed in the standard period}^*}$$

Obviously a company that has increased its capital by the retention of profits alone is the victim of serious discrimination. In fact, a company from which capital had been withdrawn might conceivably benefit by an adjustment of standard profits under this section, provided its accumulated profits exceeded the amount of capital withdrawn.

Apart from the question of equity it is difficult to understand the Minister's differentiation between an increase in capital resulting from retention of profits as against an increase in capital resulting from the issuance of a stock dividend. True, the capital stock is increased in the latter case but capital is not defined as capital stock by the Act. Thus, if accumulated earnings do not result in capital contributed, neither does the issuance of a stock dividend, regardless of the similarity of effect between a stock dividend and the return to the company of cash received in dividends in payment of additional stock issued.

Under the English Excess Profits Tax Act an adjustment of standard profits is made having regard to capital employed in standard and taxation periods, irrespective of how capital increases or decreases have taken place. Furthermore, capital employed in any period is adjusted for profits or losses which are deemed to have accrued at an even rate throughout the period.

In his budget speech Colonel Ralston, speaking of the original Excess Profits Tax Act passed in September, 1939, and repealed in its entirety in August, 1940, made the following statement: "In the light of actual conditions it was found that many established firms would pay little or no tax while others which had not been in business prior to the war or had been operating in a depressed industry, or were undergoing rapid expansion would be subject to what appeared to be unwarranted discrimination." In the Ways and Means Committee Mr. Ilsley is quoted

*Calculated using a simple arithmetical average.

as follows: "The profits of a standard year are subtracted from the profits of a tax year and 75% of the difference is taken. That is on the assumption that the capital remains the same. But in respect of a company which has changed its capital there must be an adjustment of those figures. If the capital of the company is changed, or if, for instance, there were $2,000,000 invested in a tax year and $1,000,000 in the standard year then it would not be satisfactory to make that subtraction because your taxation would be oppressive and entirely unfair. In other words, you would not be comparing like with like," and again, "You are taking the increased earnings per dollar invested because you are relating it to the capital. That is what I meant when I said that that is the principle underlying the taxation of ordinary industries."

It is difficult to reconcile the above statements with the harsh treatment promised by the Minister's brochure of firms undergoing rapid expansion and financing through "ploughing back" earnings.

> (c) "adjust the standard profits of taxpayers engaged in the operation of gold mines or oil wells having regard to any substantial increase or decrease in volume of production in the year of taxation as compared with the average volume of production during the standard period."

The Minister's brochure illustrates the operation of this section in the following manner: "If a gold mine had a standard profit of $10,000.00 as a result of producing an average of 100,000 ounces per year during the standard period, but doubled its output in the taxation year it would be entitled to have its standard profits doubled to $20,000.00." Thus, the only factors that will determine the liability of a gold mine for excess profits tax are the price of gold and the cost of production. The price of gold has risen from $35.00 to $38.50 per ounce, a percentage rise of 10% of the former price. This factor alone will not be sufficient to subject a gold mining company to more than the minimum tax of 12%, for as already stated, standard profits must be exceeded by more than 24.24% in the taxation period before the 75% rate is effective. It is well known that, unlike the average business, gold mines are able to exercise considerable control over their costs both by control of development expenses and by optionally mining low or high-grade ore. Such mines will find it in their interest, therefore, to maintain costs at old levels rather than reduce them.

The one bad feature in this provision from the government's standpoint is that gold mines are discouraged from mining high-grade ore

and creating the largest possible supply of gold so urgently needed for purposes of foreign exchange.

No attempt in this article will be made to deal with the problems under the Act of mines producing other metals jointly with gold.

(d) "adjust the standard profits by reference to any increase or decrease in depreciation allowances or other charges to such a basis that the said charges during the standard period are comparable with similar charges during the taxation period."

According to the Minister's brochure "the adjustment provided for in this paragraph is to be made only in the case of a material change in the basis of taxation as between the standard period and the taxation period."

It is difficult to understand such interpretation of this section of the Act. For example, a business might, in the taxation period, suddenly find itself with its machinery and equipment fully depreciated, yet still in good running order. In such a case there is no question of a change in the basis of taxation, yet this section of the Act would appear to give the Minister power to make the necessary adjustment. A concern may incur special non-recurring charges in either standard or taxation period, which have been consistently allowed under the Income War Tax Act as a proper deduction, and in such case the Minister is undoubtedly empowered to adjust the standard profits. This section of the Act need not, of course, benefit the taxpayer. Standard profits may be lowered as well as raised.

A serious omission in the Act appears to have been the provision for adjustment of the standard profits in respect of revenue or credits as well as "other charges." It is possible, however, that revenue may be considered a negative charge. In fact, the example given by the aforesaid brochure in illustrating the operation of this section of the Act is that of a taxpayer who held a large block of Dominion of Canada tax-free bonds. These bonds matured in 1937 and were replaced by taxable Dominion bonds. It was proposed, therefore, to raise the standard profits for the years to 1937 by the amount of revenue that otherwise would have been reported as taxable. Strictly interpreted, the Act would not permit of such adjustment unless a charge can be considered as negative.

5(1) "If on application of a taxpayer the Minister is satisfied,—

(a) that there were no profits in the standard period because the taxpayer was carrying on business at a loss or that

the profits of the standard period were so low that it would not be just to ascertain the standard profits of the taxpayer by reference to such profits because either the business is of a class which during the standard period was depressed or because the business of the taxpayer was for some reason peculiar to itself abnormally depressed during the standard period when compared with other businesses of the same class.

he may direct that the standard profits shall be ascertained by the Board of Referees as if the profits of the standard period were of such greater amount or such amount as they think just; provided that the decision of the Board shall not be operative until approved by the Minister, whereupon the said decision shall be final and conclusive.

(2) The standard profits ascertained by the Board, as provided in subsection one, in the case of taxpayers mentioned in paragraph (a) thereof, shall not exceed an amount equal to interest at such rate as the Board shall determine, not being less than five nor more than ten per centum per annum, on the amount of capital of the taxpayer computed by the Board in its sole discretion in accordance with the First Schedule to this Act.

A special form is now available to any taxpayer who wishes to make application to the Board of Referees for an adjustment of standard profits under this section. It is expected that taxpayers belonging to a class which during the standard period was depressed will apply to the Board through their association. According to the Minister's brochure such claims are first to be considered by himself and may be passed on to the Board for consideration; further, that "any claims disallowed by the Minister may be referred to the Board on the request of the taxpayer, and if so referred, the reference will be subject to costs to be assessed by the Board against the taxpayer if his claim is again refused." In any case, however, it should be noted that the Minister must approve all decisions of the Board.

Mr. Ilsley in the Ways and Means Committee made the statement that this section of the Act is designed to apply only in exceptional cases and that he did not anticipate that the Minister was going to apply it to a large range of industry. In other words, the effect of this section is not to guarantee every taxpayer a minimum standard profit equal to 5% of the capital invested. It is expected that companies claiming to be depressed must show that they have been capable of making a higher return on capital in years previous to the standard period.

A standard profit once established by the Board and approved by

the Minister is said to be unalterable except for future Ministerial adjustments under Section 4 of the Act.

Inventory Reserve:

6(1) "A corporation or joint stock company taxable under the Second Part of the Second Schedule to this Act shall be entitled, in respect of any taxation period, to deduct from profits the following:

(b) such reasonable provision as a reserve against future depreciation in inventory values as the Minister, in his discretion, may allow, having regard to a basic quantity of stock in trade necessary for the business as indicated by the quantity on hand at the end of the fiscal period of the taxpayer ending in one thousand nine hundred and thirty nine: Provided that no such deduction shall be allowed which provides against a decline in inventory values below the inventory prices of goods on hand at the end of the fiscal period of the taxpayer ending in the year one thousand nine hundred and thirty-nine: And provided further that any reduction in such reserve shall be added to the profits of the year of reduction for purposes of taxation under this Act."

No tax saving under the Act would be effected by a reserve against future inventory losses unless a business is subject to tax at the 75% rate, and according to the Minister's brochure "no reserve as a deduction is allowed companies not taxable under the said (75%) rate." It is not clear whether companies must still be taxable at the 75% rate after deduction of the inventory reserve from profits or whether it is possible to set up sufficient reserve to reduce excess profits to the point where companies are subject only to the minimum 12% rate.

This section of the Act will not provide any relief from taxation to businesses making profits subject to the 75% rate in the year of the reduction of inventory reserve, for the amount of such reduction must be added back to profits. It appears, however, that in any other case a business will secure a partial or full tax saving on the amount of such inventory reserve. This is illustrated by the figures set out in Schedule "A" in which four companies are assumed to have the same standard profit and each are required to add back to profits the same amount for reduction of an inventory reserve previously claimed. Where there is an excess profit less than 24.24% of standard, but the adding back of the amount of the inventory reserve reduction increases such profit to more than 24.24% of standard, it may be seen that partial relief from taxes is received. If the adding back of the amount of the inventory

reserve reduction increases the profit to a point not in excess of 24.24% of standard, then a full tax "saving" is effected.

No statement has yet been given out by the Minister as to the correct treatment of an inventory reserve provided by a company paying tax for less than a full year in 1940. It is rumored, however, that only the proportion of such reserve can be claimed as the number of months in the 1940 period bears to a twelve-month period. If this is to be the correct treatment and it were necessary in the year of reduction to add back the whole amount of the reserve created, a company would probably be wise to defer the claiming of such reserve until the year ending in 1941, unless, of course, a poor year were anticipated.

Schedule Showing the Tax Saving Under the Excess Profits Tax Act Upon Adding Back to Various Profits or Loss a Reduction in Inventory Reserve

	Company A	*Company B*	*Company C*	*Company D*
Net taxable profit or loss for 1942	$125,000	$115,000	$105,000	$ 10,000
Add reduction in inventory reserve	15,000	15,000	15,000	15,000
	$140,000	$130,000	$120,000	$ 5,000
Less standard profit	100,000	100,000	100,000	100,000
Excess profit	$ 40,000	$ 30,000	$ 20,000	$ Nil
Less allowance for income tax	7,200	5,400	does not apply*	does not apply
Excess profit subject to tax	$ 32,800	$ 24,600		
Excess profits tax payable	$ 24,600	$ 18,450	$ 12,600	$ Nil
Excess profits tax payable before adding back reduction in inventory reserve	15,375	13,800	12,600	Nil
Excess profits tax payable on amount of inventory reserve added back	$ 9,225	$ 4,650	$ Nil	$ Nil
Excess profits tax saved when inventory reserve created	9,225	9,225	9,225	9,225
Net saving in excess profits tax	$ Nil	$ 4,575	$ 9,225	$ 9,225

*Taxable at 12% of net taxable profit.

*Editor's Note: ***This article, completed by November 15, 1940, cannot be considered to take into account any revision in the Act which might be made between that date and the date of reading. As of the date of publication, there have been no such revisions.***

CREDIT CONTROL

P. M. MILLIANS

Mr. Millians elaborates on Credit Control as a means of approaching a perfect balance between risk and profit.

* * *

THE fundamental problem of Credit Control is one of risk. If we are thinking of control in the dictionary sense of "the power to regulate," then in this sense Credit Control is impracticable. Both on a basis of fact and presumptive reasoning, this statement appears to be correct.

Under our doctrine of free enterprise we have developed a rather complicated system for supplying our wants. It is a wonderful system and a wonderfully effective system when it works. But when it periodically gets out of balance, as it does with some regularity, these complicated relationships subject business to risks from which it was free during earlier periods of our commercial history.

These periods of economic disturbance bring with them uncontrollable forces which strongly influence the risk of credit.

This is not a suggestion that we seek to do anything about this particular risk, because it is an inherent part of our free economy. An effort to remove it would conceivably result in a regimented economy of some kind, in which each business would be told what and how much to make; an economy in which it would be impossible for us to distribute ourselves to occupations of our own choosing.

In addition to these uncontrollable economic forces which increase the risk of credit, there are areas of the unknown in business management which make credit control in any regulatory sense impracticable. Notwithstanding all that we hear about efficiency in business, there is still an amazing amount of drift in it. Unknown internal forces, both for good and bad, are frequently working to make or break a business enterprise.

As business has grown in size and extent of operation, investments in fixed capital have increased and profit and loss relationships, like economic relationships, have become more complicated. And as a consequence this area of the unknown in business management has been considerably widened.

Some, in fact, are now questioning whether the bigness and

complexities of business generally have not outstripped managerial capacities presently available. Mr. Justice Brandeis of the United States Supreme Court thought "there are definite and not very wide limits to the capacity of even the best human mind to manage organizations well and that, therefore, with bigness there necessarily goes both waste and inefficiency."

The unknown in business management is being greatly lessened by research and education, and there will be more and better management available to cope with the increasing complexities of business as Schools of Commerce train greater numbers. But errors are incidental to all human effort, and there will always be errors of management to make business survival less secure.

The factual proof of the risk problem in credit granting is found in the high general level of credit losses, both in Canada and in the United States, at all times, and in the constant variations in losses from year to year. Additional factual proof is found in the experience of single concerns whose credit losses move in no relation whatever to general averages or general business conditions.

Credit Control obviously does not mean to keep credit losses at some traditional percentage of sales. And even if it were possible to pick only the "good" accounts, the penalty of such an effort might be deprivation in the direction of net profits.

Credit Control, then, appears to be some kind of balance between "credit risk" and the profit possibilities of the business offered. That business generally strives for such a "balance" is evidenced by the broad relation of credit losses to profit margins in various types of business.

To a very large extent, however, "measures of risk and profit" in various types and classes of accounts are "guessed at" rather than known. Such measures can perhaps never be precisely calculated, however; precise measures are not necessary for the usual purposes of control.

Sixty years ago a young man working as a yard laborer at the Midvale Steel Company in Philadelphia was thinking about the problem of control as it applied to production processes. That young man was Frederick W. Taylor, who became a dominant force in a new management movement. Taylor in production control reduced operations, which on the surface had great variability, to standards of measure that were remarkably accurate.

During the period since about 1900 retail store management has

been working on the problem of inventory control. Filene, and others, working on inventory control, found that variables in style, color and size could be measured. The result has been an astounding reduction in inventory losses due to obsolescence, or changes in consumer demand.

In its handling of a great variety of accounts, both in kind and size, Credit Management is admittedly dealing with many variables. As an entity the over-all risk of any group of accounts embraces variables in capital structure, as well as a variety of possibilities for trouble and expense on particular accounts. From the profit angle, Credit Management deals with variables in the form of great and natural differences in the profit value of customers. And the profit content of sales dollars increases and decreases substantially at varying levels of revenue, depending upon the relationship of fixed cost to total cost in the business.

But these variables are no greater than the variables in Production, Merchandising and other departments of business, which have been measured with impressive dollar and cents results.

The common pattern of all the control methods that we read about in the literature of Management is investigation, classification, measurement. My suggestion is that Credit Management might profitably use this "pattern" in its own work.

In connection with variables in risk, there seems to be nothing to prevent a single business from accumulating some evidence to justify predictions of the kind that Credit Indemnity Companies make when they say that the chance for loss is, on the average, so much in each classification of accounts. This is true because, on a broad grouping, there is a relationship between net worth and the probability of failure that can be calculated although the principle of individual differences works in each group. Schedules prepared periodically should show credit limits, sales, losses, past due accounts, and the like in each "risk" classification.

The size of each measured group will influence the result. This is the principle of probability working on large numbers and the usual proof of this principle is the familiar coin pitching demonstration. If ten coins are pitched into the air, the probability is that one, five or even ten may fall heads-up. If increased to 100, heads would more than likely vary between 45 and 55. In other words, as the number is increased the variation in probability decreases.

It should be made quite clear, however, that the extent to which these averages will work for a single concern is limited.

The proper working of the law of average requires a wide distribution of risk over accounts of the same size and class and this condition rarely exists in a single company to an extent necessary to provide much of a safeguard. A large number of accounts is not sufficient. There must be a large number of the same type and class. For example, on size alone, assume an extreme distribution like 10,000 accounts of $50.00 each and a few ranging from $500.00 to $5,000.00 each. Several failures in the latter group would upset all the calculations of averages that could be made.

In connection with differences in the profit value of accounts, there seems to be nothing to prevent measurement of accounts on a basis of averaged profit contribution of each classification.

For such a classification factors like location and size of account would be considered. Accounts located in prime territories are less expensive to sell than those in distant territories where cost of selling is higher. Many accounts would no doubt be found producing volume below a profit point because of justifiable credit limits, there being no hope for their construction on a profitable basis. One analysis showed that accounts in the low capital group, where risks are ordinarily considered high, were relatively more profitable.

No estimate of the value such an approach to credit control would be to a particular business is offered. Obviously enough accounts would have to be involved in the study for averages to correct variations in some degree.

It seems safe to say, however, that a Credit Manager could do an infinitely better job of selecting accounts if his judgment were backed by some knowledge of how the risk in his receivables is distributed.

It seems plausible that a Credit Manager could be a more constructive profit force in his business if he were in a position to point out unprofitable accounts to the Sales Department and to draw a fine line between classes of accounts that could be constructed on a profitable basis and classes that are hopeless and should be eliminated.

The whole thought about such an approach is for the Credit Manager to get down under totals of receivables and totals of credit losses and see what can be found that will be helpful. Credit Control means that dilemma of all Credit Executives, maximum sales and minimum credit losses; the perfect balance between "risk and profit." It is believed that the measures of risk and the measures of profit suggested will, when correctly calculated and backed by sound credit judgment, result in the nearest approach to this perfect balance.

This will reduce the risk of abnormal losses, but for the reasons we have already discussed, the probability of abnormal credit losses is perhaps greater right now than in any period of our commercial history. To meet abnormal credit losses which have occurred with varying frequency and severity down through the years and which continue to occur in spite of great advances in credit techniques, Credit Insurance Companies have been organized.

Credit Insurance is not a control device, but a device for distributing credit losses that cannot be controlled. Its use to protect business against abnormal credit losses and its constantly widening use in protecting other credit risks merits its consideration in any discussion of credit control methods.

In form Credit Insurance falls into two broad classifications, "General Coverage" and "Specific Coverage." Variations from these basic forms are many, in order to meet the desires of many types of business, and the necessities of particular situations. The insured, for example, may wish to handle collections of all past due accounts and be protected only in the event of ultimate insolvency. On the other hand, the insured may wish to have all past due accounts constitute a claim under the policy contract, within some agreed period of time after maturity. Or the insured may want to go back of date of shipment and protect goods in process of manufacture. These varying conditions, and many others, require riders or indorsements on standard policy forms.

As the name implies, "General Coverage" Credit Insurance is designed to give business complete protection against all credit losses above the normal loss assumed by the insured. This normal loss is first broadly determined from the average for the class of business to which the insured belongs. The individual business within each group may, however, "merit" a normal below this broad average. Conversely, it may be necessary to "de-merit" the insured because of a sustained loss record above the industrial average.

If an explanation of "General Coverage" Credit Insurance should be squeezed down to a few words, it would be that it "levels down" loss variations and reduces one "cost" of credit to a fixed amount. Under this form of policy all the individual elements which contribute to credit risk become an entity susceptible to measurement and expression as a fixed amount.

The protection of profits and capital values is the first appeal of complete protection, though many concerns stress its value from an

accounting and financial standpoint. The idea of a fixed cost in profit planning and profit control is an important consideration with them.

"Specific Coverage," the other of the two broad forms of Credit Insurance, provides a guarantee on single accounts or groups of accounts named by the insured. These accounts for the most part represent concentration of risk in amounts larger than the insured cares to assume.

Thus we may say that "Specific Coverage" tends to "level down" risk as distinguished from "General Coverage" which "levels down" losses. As an illustration, suppose that a large part of receivables value is represented by numerous small accounts. If there is no concentration of risk in a single industry, or in one geographical area, a measure of distribution exists which admittedly lessens the chance of serious credit loss. But if the other part of receivables is made up of an assortment of accounts of more than average size, the failure of even a few of these accounts would result in serious loss. Protection of these larger accounts by "Specific Coverage" Credit Insurance "levels down" risk.

Credit Insurance, therefore, gives values in two broad ways: either complete protection against abnormal credit losses, under a General Coverage form of policy; or a guarantee of accounts representing high concentrations of risk, so as to "level risk on total receivables."

Sometimes the statement is heard that "My business can stand an abnormal credit loss." But Credit Insurance Companies contend this is not the purpose of Credit Insurance.

The value of putting a ceiling on credit losses does not revolve around the question of whether a business can stand the financial shock of a large credit loss. It is conceded that disaster may not result from credit losses unless a business is weak financially, or has a fairly high concentration of risk.

For the business that can stand the "shock" of large credit losses, complete protection against losses in excess of normal is for the purpose of that very thin profit line upon which ride all the hopes and reputation of management.

Normal credit losses are provided for by a charge to sales. But any loss in excess of normal comes one hundred cents on the dollar out of net profits. If net profit is 2% on sales—and a recent study showed this to be a good average—it would require $50,000 of good sales to offset $1,000 of abnormal bad debt losses. Or from another angle, the risk is net profit on $50,000 of sales for every $1,000 of excessive loss, a 50-to-1 shot. There is a vast difference after all between sound financial

management and gambling—and gambling with a profit at a 50-to-1 shot is not sound financial management. It isn't even good gambling.

The effort is sometimes made to meet the contingency of abnormal credit losses by creating extra reserves for this purpose. But the fact should not be overlooked that such reserves can come only out of profit, and the difference between paying abnormal credit losses out of current earnings, or out of reserves accumulated from current and prior earnings, is merely one of time.

If a business has the financial resources to create idle reserves, and assuming that management will keep the reserve inviolate despite the soft-voiced temptation to dig into it when there is urgent need for some extra cash, the case for or against Credit Insurance protection becomes one of dollars and cents. Where a business actually takes money out of surplus to create a true reserve, the earning power of such funds when employed in the business is frequently greater than the premium cost of adequate credit insurance protection.

A favorable credit loss experience over a period of a few years sometimes intrigues business. Management concludes that instead of paying a premium for protection against abnormal credit losses, a corresponding amount should be bet aside as a reserve against such an event. Numerous cases are on record, however, where credit losses during a short period have more than exhausted reserves accumulated over a large number of years.

In such cases the damage could be greater than the destruction of the reserve, as serious as that would be. Its earning power would be destroyed for all time to come. Assuming that a business is financially able to create true reserves, as distinguished from the mere bookkeeping entries, the question becomes whether the reserve and its earning power should be left unprotected, when complete protection can be purchased at a price rarely in excess of the amount of interest the reserve would normally earn.

Does this mean that Credit Control is reached through Credit Insurance protection? Far from it. What it is intended to mean is that Credit Control is far more complex than a lot of persons think. It involves two ends of a different balance, risk on one end and profit on the other. Credit Insurance completes the control pattern for it starts paying losses at a point set by the efficiency of the Credit Department of the Insured.

THE BEHAVIOR OF BANK DEPOSITS IN CANADA

MARK K. INMAN

Dr. Inman investigates actual bank deposit behavior in Canada and compares his findings with the theories of Keynes, noted English economist and expert on business cycles.

* * *

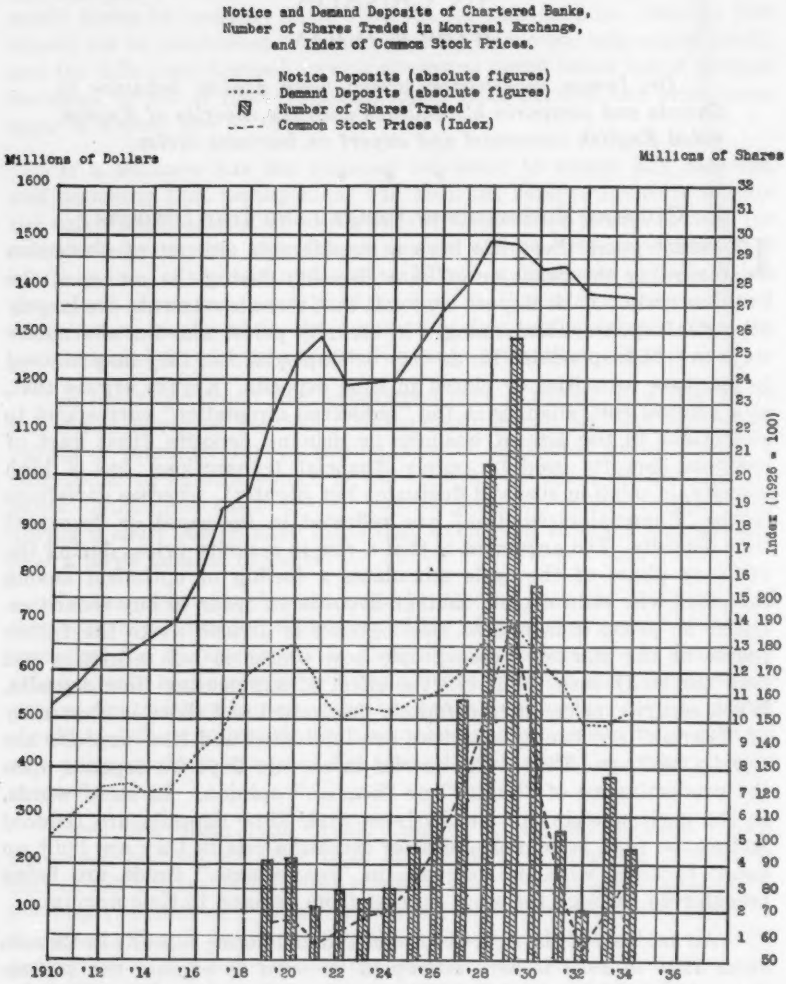
Cyclical Movements of Demand and Time Deposits

IN recent years there has been a considerable amount of discussion regarding the behavior of bank deposits during the course of the business cycle. J. M. Keynes contends that these movements are largely dependent upon cyclical changes in security prices and the alternative ways in which spendable funds may be employed, *i.e.*, they may be used to purchase securities or placed in time deposits. Keynes argues that, as a general rule, changes in the "industrial circulation" correspond to alterations in the size of business or demand deposits (that part of business deposits used in purely financial transactions, has a high velocity, is small in size and fluctuates but slightly), whereas variations in the "financial circulation" are reflected in increased or decreased time deposits. The argument is that a rise in security prices during the recovery phase of the cycle stimulates a feeling of optimism among investors who reduce their savings deposits in order to buy securities. Later, as prices continue to rise, opinion is divided as to the future course of the market. Some people now prefer to sell securities and hold (or lend) cash. This has the effect of augmenting time deposits. When security prices turn definitely downward and there is unanimity of "bearish" sentiment, securities are liquidated and time deposits are rapidly built up. Thus a fall or rise in savings deposits depends upon the predominance of "bullish" or "bearish" opinion.[1] In other words, in the early upswing of the business cycle time deposits are reduced and as the peak is neared and after recession sets in they are built up again because, with the increase in "bearishness," funds are being transferred through the stock market from demand to time accounts.

An analysis of the figures for demand and notice deposits in Canada from 1910 to 1934 is here attempted in order to explain the various movements which may be found therein, and to determine whether or not these movements conform to theory as enunciated by Keynes. The

[1]J. M. Keynes, A Treatise on Money, Vol. I, Chap. 15.

accompanying chart[1] gives a picture of the respective movements of demand and time deposits in Canada during the period which is under consideration.



[1]Source of data on which the chart is based: Curtis, C. A.: Statistical Contributions to Canadian Economic History; Canada Gazette (Supplement); Statement of Banks Acting under Charter Dominion Bureau of Statistics; Recent Economic Tendencies in Canada, 1919-1934.

An examination of this chart shows a fairly steady increase in notice (time) deposits, 1910-1921, but this growth was halted in 1922 and for a period of three years practically no gain was registered. The upward movement was resumed after 1924 and continued to 1928. Thereafter, the trend was downward. The curve for demand deposits exhibits the same general movements, except for its slump in 1914 and for the fact that the turning points do not always coincide with those of time accounts. In any case, the data gives evidence of a distinct cyclical movement. In considering the post-war years to the depression of 1921-22, it will be seen that time deposits increased rapidly in 1919 and 1920; but so did demand deposits. The inverse correlation which Keynes' theory implies is not found in this connection. So far as the turning point of the cycle is concerned, there is some evidence in support of Keynes' view. Time deposits increased in 1921, whereas demand deposits, security dealings, and common stock prices declined. In other words, "bearish sentiment" predominated during the early phase of the stock market recession. Nevertheless, both demand and time deposits fell in 1922. However, Keynes may find some consolation in the fact that common stock prices and security trading increased that year, a movement which was reflected in reduced notice deposits. Possibly the reduction in demand deposits in 1922 can be explained on the basis of a "lag" in the transference from one type of deposit to the other.

The movements of bank deposits during the period 1922-1929 also substantiate Keynes' thesis in some respects and contradict it in others. During the recovery phase of the cycle, especially in 1923, demand deposits rose approximately $20 millions, whereas time deposits increased less than half that amount ($7 millions). This indicates the prevalence of a fairly strong "bullish" opinion which, however, did not result in an actual decline of time deposits. The slight reduction of demand deposits in 1924, accompanied by a very small rise in notice deposits, is due to the industrial recession of that year. From 1924 to 1928 both types of deposits increased. In this "prosperity" phase of the cycle with its accompanying rise in security prices and sales, the prevailing feeling of optimism should have resulted in a predominance of "bullish" sentiment, thus causing a drastic reduction in savings deposits. But this reduction did not occur till 1929. In that year rising common stock prices and augmented security trading were accompanied by an increase in demand and a decrease in time deposits. The prospect of securing great gains from rising security prices lured many hitherto cautious investors to take a chance on making a "killing" in the stock market. This conduct resulted in depleted time deposits. It is important

to note, however, that this shift to the "bull" position took place late in the upswing of business, not early as Keynes' theory infers.

The course of events after 1929 lends little support to the Keynesian hypothesis. The trend in both types of deposits to 1932 was downward, whereas in order to conform to the theory under consideration, time deposits should have risen as stock prices declined. It is true that an increase of approximately $10 millions in notice deposits did occur in 1931; but this in all probability was a result of the banks' large security purchases of that year. In any case, the downward movement was renewed in 1932, when time deposits fell over $60 millions. In 1933 the decline was arrested. The following year (1934) time deposits fell slightly and demand deposits registered a gain. This may indicate a preponderance of "bullish" sentiment, but it is just as reasonable to assume that the addition to demand deposits resulted from an increase in productive activity. The physical volume of business index went up 18.2 per cent. that year, while the number of shares traded on the Montreal Stock Exchange actually declined, despite a rise in common stock prices.[1] The slight reduction in notice deposits in 1934 can be explained on the basis of a withdrawal of savings by comparatively small depositors who were attempting to maintain their standard of living in the face of continued unemployment. The increase in employment in 1933-34 as a whole was undoubtedly a major factor in arresting the rapid downward trend in time deposits after the "boom" in 1929.

With respect to the cyclical movement of time and demand deposits in the United States during the period 1910-1934, one investigator, Lawrence W. Towle, has found even less verification of the Keynesian theory than the writer of this article has been able to discover in regard to Canada.[1]

Bank Deposits, Prices, and Production

In his consideration of the relative movements of time and demand deposits in England and the United States during the post-war period, Keynes, in common with other research workers of both countries, found that the percentage of time deposits to total deposits increased almost continuously between 1919 and 1929.[2] In the former country deposit accounts (time deposits) increased from 34 to 48 per cent. of the total.[3] For the United States the percentage ranged from 24 in

[1]See Chart.

[1] "Cyclical Behavior of Time Deposits in the United States," Harvard Business Review, Winter Number, 1936, pp. 225-234.

[2]J. M. Keynes, *op. cit.*, Vol. II, Chap. 23.

[3]J. M. Keynes, *op. cit.*, Vol. II, p. 9.

1919 to 42 in 1928.[4] The almost steady increase in this item from year to year denotes the absence of a marked cyclical movement in the sense of a transfer of funds to or from time deposits in accordance with the dominance of "bearishness" or "bullishness" among investors. Keynes is apparently unconcerned with the problem of cyclical variation in this empirical treatment of the changing proportion between time and demand deposits. He contends that in his own country the operations of war finance disturbed the usual deposit and current account relationships, hence the movement in the "twenties" was in the nature of a return to normal conditions. His view in regard to developments in England is summarized in the following statement:

> "Thus there has been a progressive restoration in the proportion of deposit accounts towards the pre-war figure almost uninterruptedly from 1919 to 1929."[1]

With respect to the same phenomenon in the United States, Keynes recognizes the effect of lower percentage reserve requirements against time deposits and the greater efforts made by member banks to encourage savings accounts. He finds also that the movement was partly due to the pursual of a vigorous policy on the part of the Member Banks to secure this type of business at the expense of the Mutual Savings Banks.[2] Thus we see that Keynes explains the relatively rapid growth of time deposits from 1919 to 1929 primarily on the following basis: in England, a natural reversion to the pre-war proportion between deposit and current accounts; in the United States, competition among Member Banks to secure increased savings deposits owing to the lower reserve requirement for this type of account. Keynes draws the conclusion that the movement operated as a "concealed measure of deflation."[3] So far as England was concerned, total deposits were no higher in 1920 than in 1926, but current accounts were 16 per cent. greater in the former year and the gradual transfer to deposit accounts during the period resulted in a price level decline. He argues that since production was smaller in 1926 than in the early "twenties," the fall in prices was due to a decrease in current accounts.[1]

Canadian experience relative to changes in the character of deposits and in prices does not conform very closely to that of England and the United States. Developments in Canada along these particular lines are portrayed in Table I.

[4]*Ibid.*, p. 15.
[1]J. M. Keynes, *op. cit.*, Vol. II, p. 9.
[2]*Ibid.*, p. 17.
[3]*Ibid.*, p. 10.
[1]J. M. Keynes, *op. cit.*, Vol. II, p. 11.

A study of this table reveals, first of all, that there was no gradual recovery of time deposits from a "war depletion to their normal pre-war proportion." In fact, the percentage of time to total deposits was higher every year from 1919 to 1934 than it was in 1913. Nor was there any unusual incentive on the part of the banks to encourage the growth of time deposits due to lower legal reserve requirements as in the United States. The Canadian chartered banks, like the joint stock banks of England, were not compelled to differentiate in regard to the size of reserves held against time as contrasted with those held against demand deposits. Moreover, there was no apparent reason why the banks should have changed their reserve policy during the post-war years for the purpose of stimulating the growth of savings deposits.

It is evident also that the "concealed measure of deflation" resulting from a shift to time deposits, which occurred in England and the United States, was practically absent in Canada. True, as in the other two countries, the price level was lower in 1926 than in 1920. But, since there was no conspicuous growth in the proportion of time to total deposits, the fall in prices must be explained on other grounds, *e.g.*, a slight reduction in the velocity of circulation (as shown by the index for bank debits) and an increase in production. Apart from events in

TABLE I

Bank Deposits, Wholesale Prices, Bank Debits and Industrial Production in Canada

Year	Index of Total Time and Demand Deposits (1926=100)	Percentage of Time Deposits to Total Deposits*	Percentage of Demand Deposits to Total Deposits*	Wholesale prices (1926=100)	Bank Debits (1926=100)	Industrial Production (1926=100)
1913		63.0	37.0			
1914		65.5	34.5			
1915		65.8	34.2			
1916		64.5	35.5			
1917		66.5	33.5			
1918		62.2	37.8			
1919	92.2	64.4	35.6	134.0	90.0	65.5
1920	100.0	65.5	34.5	155.0	109.4	69.9
1921	97.2	70.0	30.0	110.0	94.0	60.4
1922	89.5	70.3	29.7	97.3	87.5	76.9
1923	90.8	69.6	30.4	98.0	93.4	83.8
1924	90.3	70.1	29.9	99.4	89.5	82.4
1925	95.1	70.5	29.5	102.6	92.6	89.7
1926	100.0	70.8	29.2	100.0	100.0	100.0
1927	105.3	70.1	29.9	97.7	118.9	105.6
1928	114.8	68.8	31.2	96.4	143.2	117.8
1929	114.9	68.0	32.0	95.6	153.7	127.4

1930	108.3	69.6	30.4	86.6	123.5	108.0
1931	106.5	71.3	28.7	72.1	104.0	90.4
1932	98.3	73.9	26.1	66.7	85.1	74.0
1933	98.6	73.8	26.2	67.1	98.8	76.8
1934*	99.9	72.8	27.2	71.6	99.9	93.6

SOURCE: "Original Monthly Statistics of Chief Economic Importance 1919-1933," published by the Canadian Department of Trade and Commerce.

*The percentages for each year and indexes for 1934 were calculated from figures contained in the *Canada Year Book*, 1934-35.

1921, when the percentage of time to total deposits rose from 65.5 to 70.0 and wholesale prices fell from 155 to 110, there was little in the Canadian situation, 1919-1927, to support the Keynesian conception of hidden deflation. It is interesting to note that in a majority of the years 1919-1925, prices and total deposits, and not necessarily the proportion of demand deposits, moved in the same direction. This suggests a "blurred" line of demarcation between notice and demand accounts in the Canadian banking system. Both types of deposits were checked against freely during the period under consideration, hence the tendency towards a direct relationship between total deposits and the price level.

Banking and other economic factors fluctuated in such an uncertain manner during the years 1928 to 1934 that it is difficult to generalize in respect to the influences at work. According to the figures here presented, wholesale prices fell in 1928 and 1929, but total deposits, the proportion of demand deposits and bank debits increased. The explanation is twofold: increased productivity and speculation in a rising stock market. The latter is particularly relevant to the phenomenal increase in bank debits. From 1930 to 1932, inclusive, prices continued to fall, accompanied by a decrease in total deposits, the percentage of demand deposits (a point for Keynes), and bank debits. These factors were apparently more than sufficient to counteract the decrease in production. During 1933-1934 the wholesale price index moved upward. There was also a slight increase in total deposits and the proportion of demand deposits, plus a considerable rise in bank debits. The influence of these agencies tending toward higher prices was partly absorbed by increased production. Thus we see that, during the period 1928-1934, a shift from demand to time deposits, or vice versa, was one, but only one, of several factors exerting an influence upon the course of prices.

TIME DEPOSIT MOVEMENTS AND THE NATIONAL INCOME

A statistical inquiry reveals that the movements of notice deposits in Canada have been closely related to variations in the size of the

national income. The decidedly upward trend in time deposits from 1910 to 1928, as shown in the chart, is indicative of Canada's expanding economy. In a young and growing country, this is to be expected. Demand deposits, of course, also increased. Even in shorter periods it is not unnatural to anticipate that an increase in demand deposits will be accompanied by a rise in time deposits. Demand deposits tend to expand with an upward movement in economic activity. An increase in economic activity means greater employment, rising wage rates, and larger corporate profits; hence a greater dividend distribution to stockholders. The increase in the amount of money held by the laboring and stockholding classes will result in larger savings and, therefore, augmented time deposits. The estimated national income of Canada from 1920 to 1933 is set forth in the table which follows:

TABLE II

Estimate of Canada's National Income as Based upon the Survey of Production

(000,000 omitted)

Year	Income	Year	Income	Year	Income
1920	$5,523	1925	$5.178	1930	$5,100
1921	5,215	1926	5,600	1931	4,100
1922	4,520	1927	6,101	1932	3,370
1923	4,639	1928	6,342	1933	3,340
1924	4,643	1929	6,072	1934	....

SOURCE: *Canada Year Book*, 1936, p. 885.

A comparison of Table II with the chart shows that notice deposits and national income moved in the same direction practically every year from 1923 to 1933. As the national income increased after the slump in 1921-22, time deposits, as well as demand accounts, expanded. This upward movement continued to 1928. It is important to note also that the years characterized by a rapid rise in national income were, as a rule, those in which an unusually large expansion of time deposits took place. This was particularly the case in 1925, 1926 and 1927 also, to a lesser extent, in 1928. The reduction in national income during 1929 and the years immediately following was accompanied by a downward trend in time deposits. The tendency for such accounts to vary directly with fluctuations in the size of the national income undoubtedly had a modifying, if not a neutralizing, effect upon the cyclical movements which, according to Keynes, should have occurred as a result of a shift from one type of deposit to another in harmony with the prevailing psychology of investors.

The relation between national income and time deposits in Canada

also accounts to a considerable degree for the fact that in this country the proportions between time and demand deposits did not conform to the pattern established in England and the United States between 1919 and 1929. The "prosperity" of the war period resulted in a rapid growth of Canadian savings accounts. Relatively idle deposits were not depleted, as in England, to help finance the war; on the contrary, they steadily increased. In only one year, 1918, was the percentage of time to total deposits materially reduced, and this was due, not to an absolute decrease in savings, but to a relative increase in demand deposits. The upward trend in economic activity and savings accounts was temporarily arrested by the primary post-war depression of the early "twenties" but reappeared in marked form during the years 1924-1928. Apparently the thrifty habits of the Canadian people were not altered in the decade following the Great War; although, as already noted, there was a shift to the "bull" position in 1929. In any case, it is quite evident that the size of the national income and the saving propensities of the public have exerted a major influence upon the movement of time deposits in Canada.

SUMMARY AND CONCLUSIONS

The chief results of this study respecting the behavior of bank deposits can be presented in summary form, as follows:

(1) The movements of notice and demand deposits in Canada from 1910 to 1934 indicate a distinct tendency to cyclical variation in both accounts. As a general rule, the movements did not conform closely to Keynes' theory of a shift from one type of deposit to the other in accord with "bearish" or "bullish" sentiment among investors. There was, however, some evidence in support of his view, especially near the turning points of the cycle. But in general the movements can be explained on other grounds.

(2) In Canada there was no continuous growth of time, relative to demand deposits, 1919-1929, such as occurred in England and the United States. Consequently, any decline in the Canadian price level cannot be attributed to "concealed deflation" of this character. The downward trend in wholesale prices can be ascribed to other causes, particularly the general increase in production and security speculation relative to the growth of bank credit.

(3) From 1929 to 1934 there is more evidence than in the pre-depression period of some variation in the price level as a consequence of a shift from one form of deposit to another. A change to notice deposits had a deflationary influence, 1930-1932; and to demand

deposits an inflationary effect, 1933-1934. Nevertheless, this was only one of several factors affecting the course of prices.

(4) There has been a very close relation in Canada between the movement of time deposits and the size of the national income. In general, they vary directly both in long and in short periods. This relationship has tended to mitigate the effect of other influences on time deposit movements such as a shift from time to demand deposits, or vice versa, as a result of changing opinion among investors regarding the future course of security prices. Judging from the data here examined, variations in the national income was a major factor in determining the movements of demand and time deposits in Canada during both the war and post-war periods.

TYPES OF THOUGHT

FRANKLIN DAVEY McDOWELL

Five centuries ago Johann Gutenberg assured the Development of modern ideas by his invention of casting movable types. Our 20th century civilization, of which we are justifiably proud, is in large part due to the evolution of printing and our debt to Gutenberg, the father of modern printing, should never be forgotten.

* * *

IT is in this year, 1940, that we celebrate the 500th anniversary of the invention of printing.

The art of printing has been acclaimed as one of the most important inventions known to mankind. Indeed, its origin is so obscure that it is somewhat doubtful if we may use the word *invention* with any degree of accuracy; rather *evolution* more properly might be substituted for it. The road is a far one from the rude woodblock of ancient Chinese witchcraft to the modern press, and this development was made so slowly that any so-called "invention" well could be considered as an adaptation, or amplification, of a principle previously established.

To trace this evolution down through the ages is to wander in centuries of doubts and conjectures, to seek out shadowy figures that lurk in old men's tales. Not until we turn to the court records of historic Strasbourg does the figure of one man stand out boldly against the vagueness of the background: he is Johann Gutenberg, formerly of Mainz, purported to be a member of a guild of goldsmiths and an experimenter with metals for the making of types.

We find that in the year 1439 an action was brought against him in the Strasbourg court on the charge that he "had concealed several arts" from his partners in a printing business. Just what these "arts" were is not known, but a study of the trial documents shows that whatever process Gutenberg had developed it was considered to be of potential commercial value and one that his partners were anxious to obtain.

Further testimony indicates that this secret involved a certain process of printing unknown to his contemporaries. We read that Gutenberg is charged with warning his brother not to "show the press to anyone," but that "he (the brother) should take great care and go

to the press and open it by this means of two little buttons, whereby the pieces would fall asunder. He should thereupon put those pieces in or on the press, after which nobody could see or comprehend anything."

This statement, by itself, might mean much or little. It is not more informative than that of Mathias Palmiere, of Pisa, who continued the *Chronicon* of Eusebius, and wrote, "By Johann Gutenberg, citizen of Mainz on the Rhine, an ingenious man, the art of printing books was invented in 1440."

More definite is the statement of Guillaume Fichet, Master of the College of the Sorbonne, that "They say it was indeed there, not a great way from the City of Mainz, that there was a certain Johann, named Bonemontanus (Goodmountain or Gutenberg), who first invented the art of printing, by which not with a reed (as did the ancients) nor with a pen (as we do), but with brass types books are printed, and that speedily, elegantly and beautifully."

Here arises the inevitable question: Just what did Johann Gutenberg invent? Was it the "art of printing books," or was it movable types?

In Gutenberg's own day there appeared to be a controversy raging as to the nature of his invention, if any. Even the claim that he invented movable types was contested; but there is strong contemporary testimony to indicate that he did more than this: he invented the process to cast movable types.

We have here three claims made in behalf of Gutenberg to consider. If we take the sweeping statement that he invented the art of printing, and examine it historically, doubts are raised which are all but certainty in negation. On the other hand, should we accept an equally doubtful claim that he invented movable types, it could be argued that his relative contribution to the craft involved no greater forward stride in mechanical development than the adaptation of steam power to the press, or electrical energy to the press and the composing room; for these introduced methods of production equally sweeping in their revolution of the printing industry. But the process of casting movable types was a different matter. It involved original research and experiment in both the subject of moulds and of an alloy hard enough for practical use but not sufficiently hard to cut the paper under the pressure of the press. This was a discovery which reduced the basic costs of printing and put it upon a sound, commercial basis.

I fancy that could the shade of old Johann Gutenberg come to us, we should find that he would feel more highly honored to be remembered for his process of casting movable types than for any other questionable distinction. To be the one man in all the millions of Europe to recognize the next logical step in the development of printing, and to take it, is a true mark of genius.

To touch however briefly upon the origin and development of printing throughout the ages is to support the theory of an evolution from one definite forward step to another. True, these steps were frequently faulty and sometimes far apart; but they were progressive steps. If we draw aside the curtain of time and peer down those indistinct pathways of the past, we can discern the crouched figure of the Chinese symbol carver. He is a secretive fellow, practising his art in seclusion; for his art is witchcraft and his seal, it was believed by the superstitious peasantry, carried the power to blight crops or live stock.

Close by this malevolent woodworker might be distinguished yet a second figure. The two afford us a study in contrast from dim antiquity. This second man is by way of a scientist and benefactor of his fellow-men: he is the world's first papermaker. The charm and the paper made a complementary alliance. The imprint of the one stamped upon the other opened a profitable field of exploitation, and its use was extended to embrace both people and implements. In course of time, the woodblocks advanced to things of rare beauty, and, to save labor and cost of cutting, seals were made detachable, so that a sign to blight rice crops could be substituted for that to kill hogs or even the farmer himself. With this development, evil as it was, we see the first faltering step taken in the art of printing.

The door of the 1st century closes behind us. There is nothing more to see. A people whose writings had stopped at ideographs could do nothing more with the prodigious idea they had stumbled upon. It had to wait for those who had progressed to the rational and convenient abstraction of the alphabet to take the next step. It is here that the candles of the chroniclers are snuffed. There is not even a scratch of the goose-quill to help us trace out the steps taken in more than a thousand years. But steps taken there were ingenious ones. When we are next confronted with the art of printing, it has moved from the Orient to the Mediterranean and has grown from puny infancy to lusty maturity. It is the 13th century. We stand in Cairo, examining a Koran printed with movable types.

How many unknown "inventors" had worked on this development, fagged their minds and, possibly, laid aside their problems for other generations to solve, we shall never know. But in those recordless, intervening centuries the thing was done. The transition from a crude idea to a scientifically developed craft is complete. When we consider the regular exchange of ideas and commerce that flowed from Asia to Europe during the Middle Ages, it becomes more and more difficult to accept the theory that the Western World discovered printing independent of the East.

It was not until two centuries later that printing came to Europe, and Europe was ready for its coming. When we consider the host of new ideas developing, regardless of frontiers and languages, printing had not come an hour too soon; otherwise, these ideas might have perished in that deadly frost of intellectual stagnation that comes of the night of complacency and ignorance. As it was, we observe one of those curious truisms of history, that great strides are taken at the opportune time: the hour invites the man — Johann Gutenberg was waiting.

Gutenberg's distinction was not without rival claimants. The chronicles of the period are spotted with these claims and counter-claims. We find such names as Lourens Coster, of Haarlem, and Jan de Printeur, of Antwerp, in the Netherlands; Joannes Brito, of Bruges, in Flanders; and others, all contending for recognition. Some of these were wood engravers, who printed from their own blocks by use of a roller, although generally described as "printers"; others present their case with no more solid foundation than that based upon hearsay and tradition. In the Strasbourg court records we read details of the action brought against Gutenberg by Georg Dritzehem, in behalf of his deceased brother, Andreas Dritzehem, and other partners, Hans Riff and Andreas Heilmann. It is a striking commentary upon the German people that these records, in themselves priceless documents of their cultural genius, should have been destroyed when the Prussians occupied that ill-fated Alsatian city during the Franco-Prussian War.

André Blum, in his admirable work, *The Origins of Printing and Engraving* (translated by Harry Miller Lydenberg), finds that a "study of the documents of the Strasbourg trial leads many German scholars to conclude that the secret work then engaging Gutenberg, and his three associates, was the developing of a press, the prerequisite for typographic impression. Two pieces of contemporary evidence would seem to point to such a state of affairs some twenty years before the appearance of the first, dated printed books."

It is a fact that no printed book bears Gutenberg's name and that "the first book dated and signed is the Mainz *Psalter,* its colophon naming that city and giving the date as 14 August 1457; and mentioning the names of Johan Fust and Peter Schoeffer." This Schoeffer was a son-in-law of Fust, who, through financial support to Gutenberg, became, in 1450, his "silent" partner. A curious document in the University of Gottingen gives further details of this partnership. It records that the contract was made when Fust loaned Gutenberg eight hundred florins, a considerable sum in those days, for the purpose of doing typographic work. It is possible that Gutenberg's experiments were not entirely successful and Fust, to protect his investment, advanced a further sum, forcing his son-in-law upon Gutenberg as a partner. Schoeffer may have succeeded in producing a mould which would cast letters separately. With Fust's investment, and his son-in-law as an additional partner, it would not have been difficult to force Gutenberg out of the business.

Schoeffer's activities as an inventer are commented upon by the Abbé Trittenheim, who wrote that "Schoeffer, an ingenious and skilled workman, found an easier way of casting type and perfected the art as it now exists." In a dedication to the Emperor Maximilian of a German translation of Livy, published by Johan Schoeffer, who had succeeded his father in the printing business, we read: "In which city (Mainz) was first invented the wonderful art of printing by the skillful Johann Guttenberg, in the year one thousand four hundred and fifty after Christ's birth, and there improved and perfected by the zeal and labor and with the funds of Johan Fust and Peter Schoeffer, at Mainz."

As M. Blum writes: "Gutenberg seems to have been the first to use movable types cast in metal, to have received financial aid from Johan Fust, and his process seems to have been perfected by Schoeffer."

Gutenberg's permanent memorial will remain the *Gutenberg Bible,* the most coveted printed book in the world.

Johann Gutenberg took the written word from the scribes and monastic chroniclers and made of it something more than a craft: he made it an art-craft. To appreciate the revolution which he effected in the manuscript and its production, we must examine briefly the period just prior to his birth, at the close of the 14th century.

In English literature we find this period to be of peculiar interest, for we see the rise of the "best sellers" even before the appearance of the printed word. From this we may assume that the public were

eagerly awaiting some medium, they knew not what, which would give the written word a wider circulation. These "best sellers" were only two. It is equally interesting to note that one was written in prose and that the other was after the heroic tradition in alliterative verse.

This was the age of Chaucer. Of more importance, it was the age of Langland and Wycliffe, two of the greatest evangelists of modern ideas. If we accept Geoffrey Chaucer as the "Father of English," then we must accept William Langland, cleric in the lower orders of the Church, and John Wycliffe, theologian of Oxford, as architects of public opinion who were to bridge the "Stream of Time" even to our own day.

Wycliffe, certain historians hold, brought the Bible to the common people. Other historians have challenged this statement. The dispute is one in which we have no interest here. The facts under consideration are that pictures on church walls and in church windows were commonly called the "Bible of the Poor" and that to advance his ideas Wycliffe had his "poor priests" tramp barefooted from town to village to preach on texts and read passages from such portions of the Bible that he and his scribes had translated into the English tongue. These transcriptions from necessity were made by hand, and the cost of a single copy of a Wycliffe Bible, even in those days of cheap money, was equivalent to "a load of hay."

In the background of the Wycliffe Bible we find the germ of the future circulating library, for arrangements were made among people to pay a stipulated sum for the loan of a copy for an hour a day. How many copies of Wycliffe's Bible were made is not known. It is significant that, despite organized suppression and destruction, one hundred and seventy copies have survived for more than five centuries. This is remarkable when we realize that the large majority of these Bibles are "of pocket form and were obviously intended for common folk and for daily use." Even in manuscript form, and costly to produce as it was, we find that the Bible was the "best seller" five centuries ago as it remains today.

Langland might properly be called, as R. W. Chambers points out in his splendid book, *Man's Unconquerable Mind,* " 'The Morning Star of the Reformation' with more truth than Wycliffe, whose outlook was in many ways very medieval . . . and I conceive that the Morning Star belongs rather to the day than the night."

"Long Will," as Langland names himself, wrote only one work, *Piers Plowman.* He labored upon its revision and amplification over a

period of almost forty years, and reluctantly laid aside his pen just a year before the presumed date of Gutenberg's birth.

We do not know *Piers Plowman* today and that is our loss. It has been neglected because we no longer appreciate allegory and alliterative verse, once so popular among the gentry of the North and West of England, died out in the Tudor days. All this notwithstanding, *Piers Plowman* is one of the great religious epics in the English language and it made articulate the thought of the vast, inarticulate masses of England.

Its success was instantaneous. "Long Will" was a fearless fellow who hated sham. Not even a Kipling could coin phrases more pungent in condemnation. His description of the life and times of England in the latter half of the 14th century makes his work a priceless historical document, and he shows a profundity of thought that ranged far beyond the confines of his day and period. Historically, the poem occupies a peculiarly significant niche in our annals, for the chief character, Peter the Plowman, became a symbol of the Peasants' Revolt, in 1381, which opened the era that is now all but closed.

The first version of *Piers Plowman*, written about 1362, preceded Wycliffe's Bible by two decades. Therefore, it may be acclaimed as the first "best seller" in the English language. We know of at least fifty copies made of the various manuscripts. How many more perished with the centuries is beyond conjecture. We may view the position of Langland as a popular author with truer understanding when we recognize that he was the Kipling of his day and that Chaucer was the "court poet," or Poet Laureate.

Langland held the affections of the man in the street, or in the field, as Rudyard Kipling did at the high-tide of fame, even though Alfred Austin was Poet Laureate. The analogy may be carried further. In Langland's day of costly manuscripts, the expense of making a single copy of *Piers Plowman* would be comparable to producing an edition of Kipling's poems. The fifty extant manuscripts of *Piers Plowman* show that Langland's popularity must have been enormous. This is emphasized when we remember that the population of England was then under three million, with a literacy ratio of less than ten per cent. Furthermore, Langland did not write for the wealthy classes who could afford literary luxuries: he wrote for the common people who had but in small measure the comforts of life.

The printing press eliminated the difficulty of manuscript reproduction. Gutenberg's process spread as a grass fire throughout Europe.

Within a decade of its perfection we find presses working in the Netherlands, Switzerland and Italy. The printing press was not introduced into France until 1470. It crossed the "Narrow Sea" to England in 1476, where, at the sign of the "Red Pale," at Westminster, Caxton set up his plant and ran phamphlets from the press. A year later the first English book was produced. This was Lord Rivers' translation (revised by Caxton) of *The Dictes or sayengis of the philosophres.*

It was inevitable that Caxton should cater to the tastes of the upper classes and that Chaucer's works should be published. This did not mean that Langland was forgotten. *Piers Plowman* was recited in hut and cottage. The fact that the poem boldly proclaimed that the King of England ruled by the "might of the Commons" did not commend it to the champions of the Houses of Lancaster or York during the Wars of the Roses. When, more than a century and a half later, *Piers Plowman* was published, during the comparatively mild reign of Edward VI, three editions were sold out within a year. Its doctrine met with open hostility by the House of Stuart, unbending upholders of "Divine Right," and this, coupled with the decline of alliterative verse, consigned *Piers Plowman* to comparative obscurity, although it has been known to every generation of Englishmen and reprinted numerous times. Such was the fate of the first "best seller," which, in its day, set men's minds aflame by the introduction of new ideas.

Caxton launched the printing press upon a career of five centuries of useful service in the dissemination of ideas throughout the Anglo-Saxon peoples. Its progress has been carefully recorded and it is an interesting sidelight upon a democracy that in no country has the freedom of the press been so early established, nor so tenaciously upheld as in England. This battle for freedom of thought and expression was fought within the Houses of Parliament and without, sometimes upon open fields of rebellion; but upheld it was. As a result of this, printing has been logically developed. We can trace its steps at a glance — the literary pamphlet, the book, the political dodger, the news-letter, and, finally, the great daily newspaper, bringing the news of the world to the doorsteps of the nation.

Not in five centuries has man improved upon the principle that Gutenberg devised. The radio, it is true, has taken speech and flung it upon the wings of the air. But radio's chief feature is to be found in speed of transmission. Nor is it without marked limitations. Among these are lack of permancy and compactness of record. Not even the invention of television, with its accompanying facsimile, will overcome this defect.

It is unimportant from the viewpoint of human progress whether Gutenberg invented printing for the Western World, conceived the idea of movable types, or developed the process for the casting of them. The important fact is that his genius gave to us the perfect medium for the dissemination of ideas. He made the copyist a typesetter, the illuminator an illustrator. His movable types made the printed word link the world together in thought.

Johann Gutenberg belongs to the world. Caxton and Langland belong to the Anglo-Saxon peoples. It is strange that these two, who opened the door to a new era should not be universally honored as among the truly great of our race.

RESEARCH SECTION

The following pages bring to light a portion of the original work which is being carried on every day by the

"Research Bureau"

of the University of Western Ontario, Department of Business Administration.

CONSIGNMENT SELLING

E. W. CARLTON

The growing importance of the consignment plan of selling in Canadian industry makes a knowledge of its many implications essential to everyone interested in selling. In this study Mr. Carleton has made an exhaustive survey into practically every class of product retailed in Canada. More than forty sales managers and executives in the retailing and manufacturing field were interviewed. From this wealth of information the writer has made his authentic and timely study.

The subject has been considered under several headings. First of all there is given a definition of the subject, together with explanations of other deferred payment plans. The most important feature of the study, however, is the treatment of internal control of consigned stocks, inadequate control records having frequently forced many manufacturers to abandon consignment selling. The system explained in this connection is considered one of the most efficient in Canada and has developed through a process of continual revision. In dealing with the legal implications of selling goods on consignment, Mr. Carleton was impressed by the fact that all companies stressed the legal aspect of the problem as giving manufacturers the most trouble. The able assistance rendered by Mr. J. C. McFarlane, K.C., Toronto; Mr. Frank Curran, Barrister, London; and Mr. E. Greig, Vice-President, Canadian National Carbon Company, Toronto, gives authority to the findings related to the problem. In other portions of the study similar authority was given by the experience of business executives.

* * *

What Is Consignment Selling?

GOODS forwarded by a manufacturer to a wholesaler or a retailer for the purposes of warehousing and ultimate sales are described as a consignment. In other words, the manufacturer retains ownership of the goods until they are sold by the agent. The agent, at predetermined intervals pays the manufacturer for the quantity he has sold.

Following the period of reckless spending which came to an abrupt termination at the close of 1929, many dealers found they were unable

to collect outstanding accounts after that period and, therefore, were unable to purchase stock for re-sale. They were also cut off by the banks from further extensions of credit. As a result a number of manufacturers and wholesalers, seeing their source of distribution diminishing, availed themselves of the consignment plan of merchandising. This does not mean, however, that the consignment plan started at this time, but the situation was such that many firms were forced to adopt this method of product distribution.

Before the retailer can obtain goods, he must enter into a contractural agreement with the manufacturer. There are three major types of agreements by which the dealer and the manufacturer may draw up a contract.

(1) The trust agreement,

(2) The fidelity bond agreement,

(3) A contract guaranteeing dealer's performance of the contract.

(1) *The Trust Agreement*

A definite agreement entered into between the consignor and the consignee whereby the latter contracts to handle the consignor's merchandise provided that it is placed with him in trust. The agreement emphasizes that fact that the shipper retains ownership of the merchandise, and that it shall be sold only for cash. The cash realized on the sale of the merchandise, less the consignee's commission, becomes the property of the shipper and can only be held by the consignee in trust until such time as it is transferred to the consignor. This agreement protects the consignor only to the extent that, should a dealer fail to perform his duty under the agreement, he becomes liable to prosecution under the Criminal Code. It does not make good the loss of funds occasioned by the dealer's default.

(2) *The Fidelity Bond*

The consignor can secure a Fidelity Bond on the consignee on the strength of an agreement, as outlined in No. 1, and in this way protect himself from actual loss of funds misappropriated by the consignee. The difficulty of proving misappropriation, however, is placed upon the consignor, and it is impossible to recover for merchandise released on credit. In other words, to procure settlement from the company issuing the Fidelity Bond it is essential to have definite proof that the dealer has received money from the purchaser for the goods, and has failed to hold his money in trust or remit it to the consignor.

(3) *Guaranteeing Dealer's Performance of Contract*

While somewhat more costly, the bond which guarantees the faithful performance of a dealer's contract is of more value to the shipper than the Fidelity Bond, especially where large sums are concerned. Under this style of bond the Bond Company will make good the loss if it can be shown that the dealer has failed to comply with the requirements of his agreement.

There are many alternative forms of Consignment Selling but there is only one absolute consignment plan. Many firms place goods on the dealer's floor whereby an agreement is reached in which the dealer pays 25% of the cost of the article and a finance company pays the other 75%. In this way the manufacturer receives his money at the time the sale is made, the dealer pays the finance company the 75% when the commodity is sold. The introduction of this type of selling has taken the place of the consigned plan and has proved very successful because the manufacturer receives his money at once and the dealer does not have to have a particularly large capital investment to carry on business. This method is now being used by many radio and refrigerator business manufacturers.[1]

Another deviation from the strict consignment plan is the Del Credere method used largely in the United States, and by the Pepsodent Company of Canada and many Canadian storage battery companies. The Pepsodent Company of Canada adopted this plan in 1937. Pepsodent sales have since been steadily increasing and the company attributes part of this success to their factor plan.[2] This plan carries through only to the wholesaler, *i.e.*, the retailers are not made factors or agents. The manufacturer places his goods in the warehouse of the wholesaler whom he has appointed agent. The wholesaler deposits a more or less nominal amount with the manufacturer, whose agent he is, to guarantee accounts. The manufacturer as the owner, allows his agent, the wholesaler, to sell only to those to whom he, the manufacturer, desires. The wholesaler agrees to act as agent, distribute to the retailer, collect for his principal, the manufacturer, and pay the manufacturer monthly, less the compensation provided for him in the contract.

The Del Credere plan differs from the consignment selling plan in that Consignment Selling means placing the goods with any customer on consignment with the manufacturer bearing the risk and assuming responsibility.

Admitted, the distribution under the Del Credere plan is not as

[1] W. A. Langford, Langford Radio Company, London.
[2] A. M. Stenerson, Sales Manager, Pepsodent Company of Canada, Toronto.

dense but the manufacturer has the advantage in that he may select the factors he knows are competent and have good credit ratings. Also, any wholesaler found guilty of price cutting can easily be removed as a factor for the manufacturer.

Also in existence there is what is known as "Deferred Payment" selling, which has many similarities to consignment selling. In fact, from a sales and collection aspect the result is about the same. However, from a legal angle there is a very decided difference. In deferred payment selling the goods are shipped to dealers and billed on a sales invoice. The terms, instead of being marked 2% - 10th of the following month, are marked "D. P.", and the basis of the policy is that, although the dealer is billed with goods delivered to him, he only pays for the difference between his ledger account and the inventory of goods which he has on hand.

The main difference between the deferred payment plan and consignment selling is legal. It will be noted that, when goods are shipped on consignment, a regular invoice is not made out as in the deferred plan, but a memo is made stating that the goods are shipped to "The Blank Tire and Rubber Company of Canada," care of John Smith, Kingsville, Ontario. In this way the dealer can at no time claim ownership to the goods because he does not possess any invoice stating that such goods have been sold to him.

Internal Control of Consigned Stocks

The success of any consignment plan depends largely on the degree of control the manufacturer keeps over his stock in the hands of the distributor and his continual checking of the dealer. In an effort to give readers some idea of how much work is involved, the system of one of the largest tire and tube manufacturing companies in Canada will be used as an example.

Application for Consigned Stock

Before making any application to Head Office for consigned stock privileges, an intelligent survey of the stock requirements of the dealer must be made. This may be done by examining all the invoices in the dealer's docket. From the invoices a list of all the types and sizes of tires and their frequency of purchase is made, *i.e.*, obtaining from this list the total purchases by type and size for the year. Being guided by the minimum turnover as shown below,[1] the salesman then makes an

[1]Minimum of two turnovers per year in all Western Branches, part of Toronto Branch Territory north of North Bay and extreme northern part of Montreal Branch Territory. Minimum of 2½ turnovers per year in the following branch territories: Windsor, London, Toronto, Montreal.

estimate of the dealer's stock requirements, also he must check this list with the popularity chart for size popularity. This application is then carefully scrutinized by the Branch Manager; his decisions, coupled with those of the salesman, form the basis of the information sent to the Head Office. Their decisions will be governed by their knowledge of local conditions such as "age of cars in the district" and "purchasing power of consumers in the district." After this report has been made out, it is then copied in quadruplicate: one for the dealer, one for the salesman, one for the Branch Office and one for the Divisional Credit Manager. The dealer's copy is not forwarded to him until the branch manager has received the Divisional Credit Manager's O.K.

It is the duty of the branch manager to inspect all invoices at the end of the year to determine if the consigned stock held by a dealer is in correct proportion to the turnover and sales, and any necessary revisions should be made at the end of the year. The Divisional Credit Manager has the authority to alter any stock set-up if he deems it necessary.

The Agency Agreement

In the disposal of goods by the consignment plan the relation between the two main parties involved is not that of vendor or purchaser but of principal and agent, a relationship in which the agent using his own discretion within the limits of authority given by the principal. An analysis of a typical agency agreement covers many points which may be subdivided as follows:

(1) CLAUSES FOR THE BENEFIT OF THE PRINCIPAL

(a) The appointment of the agent and his acceptance that the goods are to be shipped on consignment only, the principal retaining full ownership of the property until sold by the agent.

(b) *Further Shipments*

Provisions are usually inserted that any further commodities shipped to the agent during the period of the agency agreement shall be subject to the same conditions as original shipments, and that the agent will return to the principal at any time any or all of the consigned stock which has not been sold. Where the commodity is the result of special engineering practices and development and certain standards must be met in the installation and use, the agent may be required to meet any such specific suggestions as the consignor may see fit to make.

(c) *Disposal of Goods*

It is quite usual for the principal to stipulate that the agent will observe certain sales rules, *i.e.*, set prices to purchasers, etc., and he

may also reserve the right to change the price from time to time upon giving notice to the agent. The usual method of agent compensation permits the agent to sell the goods at the prices named by the principal, but in remitting the moneys obtained, the agent is authorized to retain the commission percentage and remit the remainder. A further method, slightly different from the ordinary procedure, is the right of the agent to dispose of the goods at any price he may require, and authorizing the agent to keep the excess of the price quoted by the principal.

(d) *Accounting of Proceeds by Agent*

By reason of difficulty in the widespread retail distribution of goods in recording and handling the various charges incurred in the transference of goods from the producer to the consumer most agreements require the agent to assume the shipping and transportation charges, cartage, consumer sales and collection expenses, space rentals, etc., the agent's remuneration being calculated to enable him to bear these merchandising obligations.

(e) *Insurance*

While the principal may by his blanket insurance policies throughout the country cover risks of burglary, fire or water, etc., it is more usual for such responsibility to be placed upon the agent as was outlined previously.

(f) *Reports*

Agents' periodic report and remittances of proceeds upon the condition of the goods he holds for the principal usually submitted on the tenth of each month.

(g) *Re Delivery of Goods to Principal*

Further useful clauses require the agent to deliver up the goods (a) upon the request of the owner, (b) in the event of non sale, (c) upon termination of the agency, (d) upon insolvency of the agent, (e) upon transfer of the agent's business. Thus assuring the owner of continued merchandising control over his goods.

(h) *Termination of Agency by Principal*

Agreements usually stipulate whether or not the principal is allowed to terminate the agreement upon notice or without notice, for such causes as unsatisfactory sales results from the agent, his misconduct, his insolvency or his failure to meet agency requirements.

(2) Clauses for Benefit of the Agent

Clauses usually inserted in the agreement for the benefit of the agent provide as follows:

(a) Definite notice from the principal of withdrawal of authority or agency appointment except in cases of misconduct, insolvency, or transfer of financial control.

(b) Definite alignment of an exclusive district to the agent giving him protection in that area, if such is within the merchandising policy of the principal.

(c) Obligation upon the principal to supply goods to the agent upon his requisition from time to time. This may be important where the agent may know the territory better than the principal.

(d) Authority to the agent to sell the goods entrusted to him and to receive the monies for the same.

Where the principal receives all the money from the agent and the agent relies on the principal to remit back the commission it may be well then to note that the agent may have a certain lien to cover his commission or his expenses incurred on behalf of the principal, provided of course, this is stipulated in the agreement.

(e) Notice of any changes in prices will be given to the agent in sufficient time that he may act accordingly.

(f) A guarantee by the principal for the replacement of defective goods.

(g) An obligation on the principal to supply necessary sales information, technical data, advertising copy, etc., to the agent to assist him in promotion of the principal's business.

(h) A provision is usually inserted permitting the agent on the termination of the agency to deliver up the goods to the owner, relieving him of further obligations to continue the sale of them to third parties or to take them over himself.

(i) The right of the agent to cancel the agency upon certain agreed conditions set forth in the agreement.

Termination of Agency

While under most circumstances the agency agreement sets forth the particular circumstances under which the arrangement can be terminated, such as by principal upon misconduct of the agent or upon insolvency or upon failure to secure sufficient business or upon transfer of his business or upon failure to comply with various provisions of the agency appointment, or in any event, upon giving certain notice as specified, there also are the occasions where in absence of specific agreement provisions, the agency may be terminated by operation of law.

Where the agency arrangement is for a fixed time without provision for cancellation upon certain terms or definite notice, the consignee may be entitled to his commission on prospective sales during the balance of the original period agreed upon if he has been dismissed without good cause before the expectation of that period.

INSURANCE

Every consigned stock account must be covered by fire, burglary and theft insurance for the full value of stock on hand at any time. The dealer may carry his own insurance policy if he so desires, or he may ask the company to effect such insurance on his behalf.

(a) Where the dealer carries his own insurance it will fall into one of the following classes:

(1) If the policy covers his entire stock-in-trade, building premises and equipment, or only his entire stock-in-trade and equipment. What is known as a "commission clause" must be obtained from the Insurance Company and attached to the policy, providing for coverage of all the manufacturer's consigned stock. The policy must be endorsed as follows: "Loss, if any, upon the stock-in-trade up to $.............., payable to the Blank Tire and Rubber Company of Canada, Limited, as its interest may appear." The value of the maximum stock to be supplied to the consigned stock dealer at any time will be filled in in the above blank space.

(2) If the policy is written to cover only the company's consigned stock, the policy must be endorsed as follows: "Loss, if any, payable to the Blank Tire and Rubber Company of Canada, as its interest may appear."

(b) Where insurance is effected by the company.

In lieu of either of the above arrangements, the dealer may request the manufacturer to arrange fire, burglary and theft insurance on the consigned stock. This coverage does not extend to any other stock that the dealer may carry, nor to his building, premises or equipment.

Current rate of insurance service charge for consigned stock coverage is approximately 1.25% per annum, based on the maximum value of stock to the nearest even $100.00 which you will be authorized to extend to the consigned stock dealer at any time during the year. (The insurance service charge rate is subject to change without advance notice.)

New Account Insurance Application

At the time that the account is placed on a consigned stock basis, or at the time of expiration of the present insurance period, if the dealer does not carry his own insurance as previously outlined, a renewal form must be filled out and forwarded to the branch, along with a cheque for the amount of the service charge.

Handling Receipt of Insurance Service for New Accounts

When the cash for the insurance coverage is received, it is written up in a cash branch report under the caption of "Cash for Other Branches," and deposited to the Head Office General Account. If more than one payment is received at a time, it is totalled and entered as one lump sum.

From the Cash Branch Report the total cash is posted to the credit of "Cash for other Branches" in the ledger. Then on a printed form the name, address, date of expiration, amount of coverage, service charge for each new account covered, and in the "Remarks" column will be shown the number of the cash report on which the service charges collections were made.

The Head Office Accounting Department will issue a debit journal voucher to charge the Branch Sales Ledger Control, and the total of New Account Service Charge shown on the statement of insurance service charge will be posted to the debit of the "Cash for other Branches" account in the Branch Ledger.

A third copy of the insurance forms is kept and filed with others forming an insurance diary. In this way as renewal insurance service charge will be posted to the debit of the "Cash for other Branches" account in the Branch Ledger.

A third copy of the insurance forms is kept and filed with others forming an insurance diary. In this way as renewal insurance comes up reference is merely made to last year's report for full particulars.

Insurance Renewals

(a) Where the dealer carries his own policy, the insurance diary is reviewed at the latter part of each month and if any policies of this class expire during the following month the dealer is advised to have his policies renewed and the renewed policies must be forwarded to the branch office for inspection.

(b) Where the dealer carries insurance effected by the company: The insurance diary is inspected regularly to see what accounts will

require insurance renewal during the current month. If some require renewal the branch manager must decide if this customer will be kept on a consigned basis and if the insurance is to be renewed and if there is enough insurance for ample protection. A form is then made up in triplicate, listing all the accounts for which insurance is to be renewed. These renewals are kept separate from any new account. The date at which renewal is to take place, the amount covered and the insurance charge are filled in. Two copies of the form are submitted to the head office accounting department. When the form is received at the Head Office, the Accounting Department will issue separate billings for each account listed; and will show in the body of the invoice, the term, and the service charge. The Head Office then prepares a journal voucher showing the total charge to the Branch Sales Ledger Control, to cover the accounts in question. When this form reaches the Branch Office debits are posted to each ledger account listed for the individual amounts.

PART II.

Operation of Consigned Stocks in the Branch

(a) Setting up the original consigned stocks.

After the head office has returned the request for a consigned stock with their approval attached, the branch has the authority to proceed setting up the consigned stock. The dealer's account is set up in the ledger and numbered. The basis for numbering the accounts is to arrange all accounts in alphabetical sequence of dealer's name, and then number them. For example, all consigned accounts whose names commence with "A" are set up in one group. Then room is allowed for future accounts whose names begin with "A". Then the numbering is commenced. The "A's" might run from 1 to 10 on current consignments and 11 to 15 left open for future use, and the "B's" from 16 to 40 and so on. Numbering is an important item in the branch, as the major portion of the head office work on these accounts is carried out by referring to the account under this code number.

When the original consigned stock is shipped to the dealer, the goods are written up on a Branch Consignment Shipping Order. First is shown the dealer's name, address, etc. Below this is listed all the goods which are placed on consignment. It is interesting to note that the goods are shipped to the Blank Tire and Rubber Company of Canada, Limited, c/o the consigned stock dealer. Only units, types and sizes are shown on this form. No prices are shown. It will be noted that the Branch Consignment Shipping Order is not an invoice and are shipped in care of the dealer. This is the only way the manufacturer

can handle the goods and still maintain legal possession. This order memo is made out on a quadruplicate form.

Part 1 (White)—The original will be sent to the customer. The customer signs this copy for receipt of the goods and then returns this copy to the branch office.

Part 2 (Golden Rod)—This copy is for the head office and will be forwarded to head office daily.

Part 3 (White)—This copy will be kept on hand at the branch for filing purposes until No. 1 part has been returned signed by the dealer. At that time it is removed from the files and destroyed.

Part 4 (White)—Is sent to the dealer along with the goods, to act as a packer's memo.

If at any time it is desired to *increase* the consigned it will be necessary to go through the same procedure as outlined above.

If at any time it is desired to *decrease* the consigned stock, the same procedure as outlined above will be followed, except that the forms are marked "Credit return of consigned stock." Then the report is made out in red.

(b) Consigned Stock Ledger

Each branch has a consigned stock ledger account. This ledger is similar in form to the regular branch stock ledger, and as goods are shipped on consignment they are posted as outgoing in the branch stock ledger; they are then posted as incoming in the consigned stock ledger. In this way separate records are on hand at the branch to cover branch stocks and consigned stocks.

(c) Replacing goods sold from consigned stock

As the dealer sells goods from the consigned stock, he must immediately advise the branch, and order replacements. This is done by means of filling out a form issued to the dealer in pads of 25 each. The form states, "I have sold the following goods from your consigned stock in my possession. Please bill these goods to me and ship replacements for your consigned stock, which replacements I agree to accept on consignment."

Goods shipped for replacement are entered on a form only slightly different from the one used for initial shipments. The form is different in color and is a three-part continuous form.

Part 1—Is the branch and delivery slip copy for deliveries to consigned stock dealers in the branch city. This is forwarded to the dealer for his signature. This slip should then be returned immediately to the branch by the trucker.

Part 2—In the case where Part 1 is used for city deliveries, Part 2 is held by the shipper until Part 1 is returned by the trucker, both Parts 1 and 2 are forwarded to the branch office. Part 2 is used as a working sheet for pricing and extending purposes. This will be turned over to the billing clerk along with Part 1, as a basis for making up the sales invoice to cover the goods already sold to the dealer from the consigned stock.

Part 3—Is sent with the goods to act as a packer's memo.

Withdrawal Authority

Just before the close of each month the Assistant Branch Manager reviews each consigned stock account to determine the withdrawals to be authorized from the consigned stock for the following month. The Assistant Branch Manager notifies the dealer of the amount which he is allowed to withdraw. The dealer should have this notification before the first of the month which the notification is made out for. A copy of this notification form is kept by the ledger keeper who advises the Assistant Branch Manager if a dealer approaches or exceeds the authority granted for the month. If such a case arises the Assistant Branch Manager makes an immediate investigation, and if such a circumstance warrants, he notifies the dealer authorizing further withdrawals.

Amount Due and Collectible

The amount due and collectible for a consigned stock account is the total amount charged through the current Accounts Receivable ledger. This represents the charges for withdrawals from the consigned stock. The terms are regular terms, 2% 10th of the following month or cash on check-out by the salesman as required by the Divisional Credit Manager.

Dealer Inventory

According to clause 2, subsection "h" of the consigned stock agreement, the dealer binds himself to take an inventory of the unsold consigned goods on or before the 25th day of each month, and to forward it to the branch at once. This clause is enforced.

Salesman's Inventory

In addition to the dealer's inventory it is the duty of the salesman

to take an inventory of the consigned stock each time that he calls on the dealer. This inventory will serve as a check on the accuracy of the dealer's inventory. At the time the salesman takes this inventory he should make a careful check of all tires and tubes on hand to see that the stock is turning over properly and that no old stock is being accumulated and not sold. It is the salesman's responsibility to see that the dealer does not take in any old and obsolete stock for credit and place it in the consigned stock. It is also the salesman's responsibility to see that no tire stays in the dealer's stock for more than twelve months without moving unless there is some immediate prospect of selling it. If such goods are found, they are to be returned to the branch at once, and this type and size of product is *not* to be replaced in the consigned stock.

Dealer Responsibility for Old Stock

Clause 2, subsection "d" of the Consigned Stock Agreement definitely places the responsibility for obsolete stock on the dealer. This clause is inserted to make the dealer conscious of his responsibilities and he must do everything in his power to keep the stock turning over. *"The time to take back slow-moving stock is before it becomes obsolete."* The manufacturer refuses to accept the responsibility for it after it is obsolete, in view of the companies' efforts and warnings to the dealer while the stock is still in good shape.

Date Code Inventories

Twice each year, once in the Spring and once in the Fall, the salesman must take a date code inventory in duplicate of every consigned stock. One copy of this inventory is for the branch and one copy will be sent to the head office, as set out below.

The Spring inventory is taken during the latter part of April and the early part of May. Inventories will be held at the branch until all are on hand, when they are sorted by a salesman and fastened in a docket. The entire docket is then forwarded to the head office, Department of Branch Operations. At the same time that consigned date code inventories are being taken, date code inventories are taken at all British American Oil and Shell Oil Company Operated Stations. These inventories are included in the docket mentioned, but each is kept in a separate section.

The inventories are taken on the companies' inventory forms and the following information is required: The total stock of each type and size will be shown in the Quantity Column, and then any tires built before certain specific dates will be listed individually in the $ column.

If one of the tires shown in the column "Tires for Attention" is old style, then it is to be designated with old letters "O/S", as shown below.

Size	Type	Total Stock	Tires for Attention
6.00 - 16	Reg. R-1	(In quantity column)	(In $ column)
		2	(Show code date of each tire)
			807 9540/S

Just before the middle of April and July each year, Head Office supplies the dealer with the date limits by types of all tires to be shown in the column "Tires for Attention." Date code information is confidential and is not divulged to the dealer under any circumstances.

Maximum Fixed Stocks

Maximum fixed stocks are controlled by the credit department.

Price Changes

In the event of a price change it is not necessary to do anything except to use the new price on all sales billings to the dealer, which go through after the price change has gone into effect.

Conclusions

It is the writer's contention that consignment selling should not be adopted by any company until every phase of the situation has been investigated. Many companies were attracted by the plan when it was first introduced, contracts were drawn up in loose form, with the result that many manufacturers and retailers were involved in court cases. As used today, the consignment plan has only proved successful in those companies that are continually revising their methods of control and relations with dealers, so that no possible loophole may be found through which trouble may arise.

SALESMEN'S CARS

J. G. LORRIMAN

"This survey, dealing with the question of allowances for salesmen's cars, was conducted by means of a questionnaire sent to a number of Canadian companies. Their replies have been used in compiling the information contained in this thesis. In some instances direct quotations from their letters will be used to show the different opinions of the various phases of the problem. At the request of several companies who have co-operated by sending in answers to these questionnaires, there will be no mention made of any specific company by name. Companies replying were all types of Canadian manufacturers who have varying numbers of salesmen on the road. It was the purpose of this survey to get a comprehensive picture of operation on the part of the manufacturer with a small sales force as well as one with a large force. The survey was restricted to Canadian companies because it was felt that conditions under which Canadian and American concerns operated differed. The number of cars operated in Canada would be considerably fewer than those in the United States, but distances covered in Canada would be greater and costs of operation would be higher. A Canadian company would, in all probability, operate fewer cars than the American company, but the original costs of these cars, the distances covered by them and their operating expenses would be greater. The original cost is more because of the government tariffs, the distances covered greater because of the scattered population and the operating costs higher because of the higher cost of gasoline, oil, etc."

* * *

EXHIBIT 1 — OWNERSHIP

PERHAPS the most important point to be decided in fleet operation is who should own the cars, the company or the salesman.

Number of questionnaires sent	49
" " replies received	31 (64%)
" " companies from which no information is available	4
Number of companies with company-owned cars	8
" " companies with salesman-owned cars	12
" " companies with both company- and salesman-owned cars	7
Total number of cars in 27 companies (approximate figure)	1,254

Average number of cars operated by each company (of which 841 or 67.06% are company-owned and 413 or 32.94% are salesman-owned) 46

Average number of cars in fleets wholly company-owned 65

Average number of cars in fleets wholly salesman-owned 54

NOTE: These figures for the total number of cars are approximate because five companies operating salesman-owned cars did not report the total number of cars in operation. It is believed that the total number of cars in these fleets would be 200 - 300 cars.

Company Ownership

There is a tendency among the companies that operate a large number of salesmen's cars to own these cars themselves. The general reasons for this may be set down as follows:

(1) There is more control over the operation of the cars when they are owned by the company.

(2) Greater economy is obtained by means of mass buying of a whole fleet at one time and also economies can be effected through repairs and extras purchased for the whole fleet, fleet discounts and allowances on gas, oil, lubrication, tires, etc.

(3) The cars may be painted in some distinctive way, or may have advertising material painted on them without any objections from the salesman.

(4) The salesman will take the car wherever he is told to go, regardless of road conditions, whereas if he owned the car himself he might hesitate about travelling over certain kinds of roads.

(5) In many cases the salesman cannot afford to buy the car in the first place. In a situation like this the company would have to finance the car anyway, so they may as well own it themselves.

(6) The company can use the make of car which they find most economical to operate, and can use the type of car best suited to their individual needs. There are a number of companies also that are linked up in some way or other with an automobile manufacturer and therefore feel obligated to use that particular make of car. When they own the cars themselves they can be sure of the make.

(7) The company can compel the salesman to carry any samples,

dealer helps, etc., that it wishes without fear of ruining the interior of a privately owned car.

(2) If the annual mileage is in excess of about 8,000 miles it has been found by many companies to be cheaper to own the cars themselves. For mileages under 8,000 they have found it to be cheaper to pay the salesman for use of his own car.

(9) When the company owns the car they are sure that the salesman will always have a car to use when he needs it. If the salesman owns the car there may be instances where it may not be available to him because other members of his family are using it.

Although many companies operating fleets of even less than ten cars own the cars themselves, it is generally regarded by many that it is more economical for the salesmen to own the cars when the number is so small.

Salesman Ownership

In general, unless some of the reasons for company ownership, mentioned above, are overwhelming, it is found that the best way to handle small fleets is by salesman ownership. The main arguments put forth for salesman ownership are:

(1) The salesman will take better care of a car of his own than he will of a car belonging to someone else.

(2) The salesman has unrestricted use of the car outside of business hours.

(3) Where the salesmen are scattered all over the country, and it is almost impossible to centralize the servicing of the cars, it is less bother to have the salesmen own the cars.

(4) Where the fleet is small and the economies to be derived from mass buying, etc., are not very great, it is more beneficial to the company to have the salesman own the car and pay him for the use of it.

(5) Where the mileage travelled on company business is under about 8,000 miles, it is more economical to have the salesman own the car in view of the large investment by the company in a fleet of cars.

In a survey of this type made in the United States by C. B. Larrabee and Joel Lewis* it was found that for the large fleet the most satisfactory system is that which comprises company-owned cars. They found that a few sizable fleets were being operated efficiently under a

*PRINTERS' INK MONTHLY, September 17, 1936, page 69.

system of salesman-owned cars. However, the operating costs of these salesman-owned groups, where they were worked out on a scientific basis, were found to be slightly higher than the costs of fleets of company-owned cars.

Conditioning Factors

The type of salesman will also have quite a definite bearing upon the way in which the salesmen's cars are handled. Where the salesman is of low calibre—merely an "order taker"—there would be a tendency for the company to own the cars. The reasons for this are that this type of salesman probably would not be making enough money to buy a car for himself, and in all probability would not be able to pay the upkeep on the car if he did get one. A salesman of this type would be satisfied to drive any kind of car supplied to him by the company, and would look after the car only at the company's expense.

On the other hand, the salesman of a higher calibre would probably have his own likes and dislikes as to the kind and type of car he prefers to drive. Many of them might want to buy a car in the middle or upper price range and contribute somewhat to the upkeep of the car themselves just for the prestige it would give them. They would then be driving the kind of car they preferred and would probably be much more contented with doing this. This type of salesman would also be inclined to have a feeling of independence and not want to be hindered by too much control by the Head Office. They would much rather get a set allowance for the use of their own cars than to be restricted by using cars owned by the company and have to report the when, where and why of every mile driven.

The territory to be covered will also have some bearing on the ownership of the car. Where the territory is small and the roads to be driven over, good highway or gravel, it would probably be best for the salesman to own the car. Here, the mileage gone in a year would not necessarily be very great and the investment in a car by the company might be too large to be profitable. The servicing charges and repairs would not be very great in a territory such as this, and therefore the economies of large fleet ownership would not have as much effect.

In a territory where the distances to be travelled are quite long and the roads are not all of the best type, there may be a tendency for the company to own the car. If this were so, the company would always be sure of the salesman going where it wished him to go. He might not like the idea of taking his own car over some of the roads such as are found in Northern Ontario where there are very few paved roads. If

the company owns the car the salesman has no choice but to go wherever he is told. He has no excuse for not covering his territory as adequately as it is desired by the company. Although it may be harder on the car, it is of more advantage to the company to have the territory covered and take a larger depreciation on the car than not to have any contact with that territory whatsoever.

Operating Expenses of Company-Owned Cars

One of the first questions asked by a Sales Manager when considering the operation of his salesmen's cars is, "How much is it going to cost me per mile to operate?" This will depend on a great many factors such as the make of the car used, the mileage driven in a year, the type of roads over which the cars are driven, etc.

It will be necessary when discussing this subject to consider the companies which own the salesmen's cars themselves and those where the salesman owns the car separately. Let us first consider the costs of operating company-owned cars.

Of the thirty companies answering our questionnaire, fifteen operating all the way from 5 to 292 cars, own some or all of the cars. Of these fifteen, eleven of them gave the figures of their actual costs per mile, some accurate even as far as four decimal places, others only an approximate figure. These figures vary all the way from 2 cents per mile to 7 cents, depending upon such factors as the number of cars in the fleet, the various territories covered and the number of items considered as operating costs. It was found that, for companies that have a figure as low as 2 cents per mile for operating costs, no charges were added for depreciation, interest on investment, etc. This is an oversight on the part of these companies, since they should recognize the fact that their cars depreciate every day, whether they are in use or whether they are standing still.

The average cost of operating of those eleven companies that gave us accurate figures was 4.0707 cents per mile. This figure, however, will tend to be a little low, since it includes both those companies that have included depreciation and those that have not. The average operating cost for eight companies that included depreciation in their figures was 4.2585 cents per mile. The average operating cost for five companies that did not include depreciation is 2.64 cents per mile. This would seem to indicate that the cost per mile to be charged to depreciation should be in the neighborhood of about 1.6185 cents per mile. The actual cost of operating, naturally, will vary considerably and will depend upon a great many different factors. Among these

should be included the size of the car used, the mileage driven in a year, weather conditions, type of roads covered and many other variable factors. For this reason we can come to no definite figure as to how much it should cost per mile to operate. Since we can draw no definite conclusions, the best thing we can do is to consider the figures as given to us by the companies answering the questionnaire. A few of the replies follow, the companies being designated by the letters of the alphabet, and no mention being made of any specific company by name.

Company AA (owns 75 to 100 cars): "Cost to operate, of course, varies according to the season—weather conditions, type of road covered, number of stops made, etc. We suppose it would run from 3½ to 5 cents per mile."

Company BB (owns 35 cars): "Cost of operating cars is 4.3 cents per mile. This covers all costs, including license and depreciation."

Company CC (owns 6 cars): "We keep careful record of all expenses in connection with each unit, including depreciation, insurance and license, and the average cost of operation is $0.0464 per mile."

Company DD (owns 90 cars): "The average total cost of operating company cars is 4.41 cents per mile. Operating costs, including gasoline, oil, tires, repairs, anti-freeze, amount to 2.83 cents; fixed charges, including depreciation, repairs, replacement of tires, and all gas and oil."

Thus it can be seen that there are many ways for a company to figure their costs on company-owned cars. It is thought by the writer to be a definite mistake to leave out a charge for depreciation and interest on the company's investment when figuring the cost per mile. For companies that have done this, however, it may be explained in part in a later chapter on Depreciation, in which the policies of some of these companies will be shown.

The material received shows quite conclusively that the actual cost of running a car ranges somewhere between 4 and 5 cents per mile. The make of car will have something to do with cost, but it was found that in the companies that answered the questionnaire, where the cars were company-owned they almost invariably used one of the lighter class of car—Ford, Chevrolet, Plymouth or Dodge. All of these kinds were used by the companies answering, so it can be concluded that a figure between 4 and 5 cents will cover any one of these makes. Usually when the figure runs above 5 cents the company wishes to use a larger type of car.

Factors Affecting Operating Costs

There are a great many variables which would affect the cost of operating a car. Among these should be included the mileage driven in the course of a year. It was found that for the companies that owned their cars the average annual mileage would range between 20,000 and 30,000 miles, although there were several that reported mileages of from 12,000 to 15,000 and several that reported as high as 40,000 miles in a year. The farther the cars are driven in a year, the less per mile will be such fixed charges as insurance, depreciation, interest on investment, etc., whereas variable charges such as repairs may tend to be somewhat larger.

The territories covered will also affect the cost of operating a car. For the companies that reported the expenses of operating cars in various districts, it was found that the cost in Southern and Eastern Ontario, Quebec and the Maritimes was the least, whereas the Prairie Provinces tended to be the highest. British Columbia, while higher than the former districts, was not quite as high as the Prairies. There are evidently numerous reasons for this among which is the fact that road conditions are much better in Eastern Canada than in the West and also the fact that prices of gasoline, oil, etc., will vary according to provincial tax laws, transportation costs of these commodities and others.

The one company that did give definite figures on the costs in various localities reported the following: "The cost per mile varies, of course, according to the territory in which the car is used. In Toronto district, including Hamilton, London and Windsor, our total operating cost was approximately 3.25 cents per mile; in New Liskeard territory it was 7.95; in Edmonton, 6.36; and in Vancouver, 6.31 cents per mile."

One of the hardest things to control, and one which may add considerably to the cost of operating a company-owned car is the use of the car for other purposes than for business. There are very few salesmen who would drive a company-owned car all week, and when he came home on the week-end put it in the garage and not use it again until Monday morning when he went out on business again. Six companies reported that they did not make any check on the amount of driving that was done for the salesman's own pleasure. They all allowed the salesmen free use of the car outside of business hours. Six other companies reported that they allowed the salesman to use the car for his own driving, but required that he report the mileage driven for himself. In some of these cases the company requested the salesman to buy his own gas and oil, whereas in some they are charged for the use of the

car on a mileage basis. In nearly all these cases it was left to the integrity of the salesman to supply his own gas and oil or to report his mileage correctly. The difficulty of accurately checking up on this would make it necessary to leave it up to the salesman to report his own driving. A salesman who did not report this regularly would soon be found out, and would probably not hold his job for very long. Three companies reported that they did not allow salesmen to use cars for their own purposes. They all reported difficulty in checking this but usually it is done by having an accurate mileage chart of the places travelled to, and checking this against the mileage as shown on the speedometer.

In order to give some of the various attitudes taken towards this question, quotations will be taken from some of the answers sent in for this question:

" . . . the salesmen are allowed to use the cars for their private use to a certain extent. We do not check up on the mileage driven by them for their personal business but we do not feel that this privilege is abused."

"Salesmen are allowed to use cars for other than company driving for the reason that we find it very difficult to make any check on this. Most of our salesmen live on the territory and as a result we do not know exactly how much personal driving they do with company cars. Our business is such, also, that salesmen often have to work on Saturday afternoon and holidays and to reimburse them for this extra time we feel that it is only fair that we should let them have the use of the cars on Sundays and evenings."

" . . . if over the week-end we prohibit the salesmen from taking their families out in the car, we have not in any way strengthened the goodwill towards the company . . . "

"Salesmen are allowed to use the company's cars for other than company's business, but are not allowed to take them on their vacation or to make long week-end trips. The amount they are used always shows when mileage is reported and the note from the salesman received as to the gasoline to be charged to him."

The problem seems to all boil down into one of the company's trusting their representatives not to abuse the privileges accorded them in the private use of a company car. Some companies allow their salesmen free use of the company car wherever he wishes to take it. They require no report from the salesman as to the number of miles driven or the number of gallons of gasoline used, but only ask that he exercise wise

judgment in the care of the car. Other companies allow their salesmen to use the cars a little, but do not allow them to take the car off their own territories or for a long distance without the consent of the sales or branch manager. These companies must trust their salesmen to report when they use the car, because there is no means of accurately checking this. The only way a company can keep a check on the mileage driven by the salesmen is to demand a detailed report of all the places visited, and check the mileage on the speedometer against the Blue Book mileages for these distances.

Operating Expenses of Salesmen-Owned Cars

In discussing operating expenses one must also take into consideration those instances where the salesmen own the cars and the company pays them for the use of them. Here, of course, we will consider as operating expenses the amount paid by the company to the salesman. There are a great many ways of remunerating the salesman for the use of his car on company business. As many of these as possible will be discussed here. In view of the fact that there are different conditions in almost every company, there cannot be any standard method of remuneration used. The methods usually vary with the opinions of the executives in that company. Some methods may work out very well in some companies and not in others. To start out with, let us consider some of the plans used by Canadian companies which were submitted in answer to our questionnaire.

Of the companies handling their salesmen's cars in this way, ten of them pay their salesmen a straight allowance of so much per mile. These allowances vary all the way from 3½ cents to 8 cents per mile, depending on the company. Three companies reported that the salesmen were paid a sufficiently high commission on their sales to take care of their own travelling expenses. Various other methods are used, some of them being fairly complicated. Some of these will now be discussed in detail.

One of the most elaborate systems submitted is that used by a large Canadian corporation that changed over three years ago from a policy of company-owned cars to one of salesmen-owned cars. For the year 1936 they based all of their computations on the price of a 1936 Standard Ford Coupe, namely, $767.00. The salesmen were not forced to buy this type or make of car, but they were being paid on this basis. In this company the actual operating costs of the cars are paid for on a weekly allowance basis. The allowance is agreed upon with the salesman, having consideration to the territory he works, some terri-

tories costing more to run a car than others. The salesmen are required to include this amount in their Expense Report. The weekly allowances cover gas, oil, tires, repairs, depreciation, insurance and sundry other charges. The number of weeks per year that the salesman operates his car, as well as the variations in the cost of gasoline and oil over various territories are given due weight in this method of figuring allowances. Besides the weekly allowance for running expenses and depreciation, interest and insurance, this company also pays the salesman three-quarters of the cost of his driver's license. For these a special Expense Report is sent to the salesmen, which they are required to fill in. This company requires that no salesman purchase a car on any other basis than straight cash, without first communicating with Head Office.

Some of the opinions given by companies that give a certain allowance per mile, with their reasons for this, are as follows:

"When we have, on the odd occasion, allowed a salesman to use his own car, we allowed 6 cents per mile. We also allow 6 cents per mile to Executives of the company for the use of their cars. We arrived at this amount on somewhat of an arbitrary basis by taking into consideration the cost of oil, gas, tires, insurance and depreciation."

"We have different allowances for the use of the salesmen's cars in our business, depending altogether on the condition of the roads on the territory in which the salesman worked. For instance, in the Maritimes and the Province of Quebec, where the roads are not so good, the allowance made is 6 cents per mile. In certain parts of Ontario it is also 6 cents per mile, and in Toronto and the southern part of Ontario 5 cents per mile."

"This mileage allowance made to our salesmen covers gasoline, oil, repairs, depreciation, insurance and everything that has to do with the running of the car, and in a great many cases we find that certain of our salesmen trade in their cars once every year and have sufficient out of this mileage allowance to pay the difference in cash required for the new car."

"Employees who are required to use their personal car on company business occasionally, and whose territory is not great enough to warrant a company-owned car, are paid at the rate of 5 cents per mile for miles travelled on company business. We have no scientific method of arriving at this figure but by our own experience in operating company-owned cars, we feel that this is a generous rate to pay employees,

considering that these cars are also used for their own personal use and it is not considered our company should be required to pay a rate sufficiently high to reimburse them 100% for the operation of their car. Such items as depreciation (which normally represents about one-half of your total cost), insurance, storage, etc., must be paid by employees whether the car is used on company business or not. We therefore feel that we are paying considerably in excess of actual running expenses of the car."

"Salesmen operating their own cars on company business receive the following allowance:

First 8,000 miles	- - -	7 cents per mile
Additional mileage	- - -	4 cents per mile

The reason for the sudden drop in allowance after 8,000 miles is that the higher figure is sufficient to absorb nearly all the fixed annual charges over the first 8,000 miles. The allowance rate is designed to cover all normal costs of operating a car, including depreciation, insurance, taxes, repairs, tires, parking, permanent garages, etc., but excludes the cost of out-of-town garages and bridge tolls."

"We reimburse them on the basis of 8 cents per mile on the actual mileage covered."

It has been found in this survey that the average allowance per mile and the one in use by most companies reimbursing their salesmen by this method is 5 cents. This seems to be the figure at which the salesmen and the company seem to strike a happy medium. It is high enough to allow a salesman driving one of the lower priced cars to keep his car in good repair, compensate him for all gas and oil and give him a sufficient amount to be set aside for depreciation, insurance, interest, etc.

The method that appears to the writer to be most fair, both to the salesman and to the company, is that in which the salesman is paid a monthly allowance of about $25.00 depending upon type of car, territory covered, etc., and he sends in his bills for all gas, oil, anti-freeze and other expenses. The monthly allowance will be sufficient to cover the depreciation, interest and insurance charges (which, it has been discovered in this survey, amount to $250 - $300 per year on a light car) and the salesman will be compensated for all of his running expenses when using the car for business. Although there is no definite check, there appears to be more control over the car by the company when this method is used. The company can take advantage of any economies

of gas and oil consumption that the salesman gets out of his car, and the salesman does not have to worry about being able to drive his car within a certain allowance per mile. The depreciation allowance in this system is sufficient to enable the salesman to trade in his car every year, a practice which has been found most economical from every standpoint. Under this system, however, the company would have to have some control over the make of car used by the salesman.

Depreciation and Interest

Wherever cars are owned there is a constant charge going on, whether the cars are in use all the time, one-half of the time, or not at all. This is the charge for depreciation and interest on the original invested capital. This is a real charge which should not be overlooked, whether the company owns the cars or the salesmen own them. It should be charged off at a certain rate per month, the same as depreciation on buildings and other equipment. Most companies, where they own the cars themselves, set aside a certain amount each year as a depreciation charge in accordance with the regular accounting practice. There are quite a number of companies, however, who do not take the interest on their invested capital into consideration. It is a debatable point, whether this is legitimate charge or not. There is reason to believe that the investment in cars could be considered in the same light as an investment in buildings or equipment with only a depreciation charge upon them. Since some companies figure interest charges on their cars, we will discuss it here only to show the way in which some companies take account of this.

Nearly all companies that own their cars set aside an amount for depreciation in some way or other, either through a definite charge per week, month or year, or else through a charge on the mileage basis.

Where the mileage basis is used, there is usually a certain charge per mile which will include all fixed charges such as depreciation, insurance, license, etc., so that depreciation cannot be determined as a charge within itself in a case like this. One company whose cars travel 20,000 to 25,000 miles per year, figures that the fixed charges, including depreciation, interest, insurance and license, amount to .01258 cents per mile on the average. This is the amount that almost any company operating light cars such as Chevrolet or Ford might safely set aside as a fixed charge when their cars are driven from 20,000 to 25,000 miles in a year. Of course, this figure will have to be adjusted somewhat when the yearly mileage is more or less than 20,000 to 25,000.

Some of the methods in constant use are as follows:

Company BBBB: "Our provision for depreciation sets aside an amount which, combined with the trade-in value of the old unit, is generally sufficient to meet the purchase price of the replacement vehicle."

Company CCCC: "Depreciation is set up at the rate of 25% per annum and charged in equal monthly instalments. This does not mean that a car is kept for a full period of four years but we have found that the allowance on the car turned in plus the depreciation set up approximates closely the value of the car."

Company EEEE: "We at the present time are using a flat write-off of $6 per week per car."

Company FFFF: "We depreciate each car 25% the first year and 20% each year thereafter."

These companies referred to all own the salesmen's cars themselves. In the cases of salesmen-owned cars, where a certain amount per mile is paid to the salesman, this usually is considered sufficient to cover his depreciation costs. He is supposed to set aside a certain amount for a depreciation allowance himself. One of the greatest drawbacks of this method of paying salesmen for the use of their cars is the fact that the majority of them will not set aside this amount for depreciation. The same difficulty is encountered in those companies where a monthly or weekly allowance is paid to the salesmen, which is supposed to take care of the depreciation. All salesmen have the tendency, when they have the cash on hand, to spend it for immediate needs, and not to set aside any part of it for future use.

A method used by one company that uses a system of salesman ownership is as follows:

"Our method of allowing for the replacement of the salesmen's cars is to set up a standard depreciation allowance based on the price of a 1937 Chevrolet Master DeLuxe two-passenger business coupe. A monthly allowance equivalent to $\frac{1}{36}$th of the total delivery price, including standard equipment, less 3% fleet discount, plus standard accessories, is set up and credited to the salesman's account each month."

This method allows the salesman to use whatever kind or type of car he wishes, but the company pays him depreciation only on the type of car they believe most suitable for their use.

Where a system of company ownership is in effect and where there

are a large number of cars to look after, there is always the general rule they are traded at a certain time every year, but there are other methods used also. Although there is no great deal of information available on this subject, one company has an interesting method of handling this. Their method is as follows:

"We have in our organization a Car Committee, appointed by the management, whose duty it is to purchase and control the operation of all company-owned vehicles. An annual review is made by each district or department having company-owned vehicles and a full report of the district's requirements is sent to the Car Committee at a set time. This report includes all vehicles which it is recommended should be exchanged, gives the mechanical condition of the car, condition of the tires, approximate cost of repairs, actual mileage the car has travelled and an opinion from the local manager as to whether or not it is considered the car may be kept in service for another year without much additional cost. The Car Committee reviews all reports and authorizes the exchange and purchase of all vehicles. All deals are made by the Car Committee and arranged with the fleet representatives of the various motor companies who obtain appraisals. Deliveries of new cars and trucks are made from local dealers; that is, Winnipeg cars are exchanged in Winnipeg, Vancouver cars in Vancouver, etc."

INSURANCE

Government regulations require that all cars, whether privately owned or company owned, be insured for property damage to the extent of $1,000, and public liability of $5,000 for one person, or $10,000 for one accident. Property damage protects you from damage done by your car to the property of any other person (but not your own property). Public liability protects you from any damage done by your car to any other person (not yourself) to the maximum of $5,000 for one person or $10,000 for one accident. These amounts may be increased to almost any number for a little higher premium.

Therefore, all cars considered in this survey will carry at least these two types of insurance. Other insurance carried on the majority of cars, although not compulsory, includes Fire, Theft and Collision.

Insurance rates vary considerably in the different provinces of Canada, and even in different parts of one province. The reasons for this are the number of accidents recorded in a certain locality, the density of the population, conditions of the roads, etc.

Special insurance rates can be obtained for a fleet of five or more

cars. The rates for these fleets are not all the same, but are based on the experience of the insurance company with that particular fleet of cars. As a general rule, fleet rates are about 25% lower than rates on individual cars.

In all the companies submitting answers to our questionnaire Property Damage and Public Liability were insisted upon. Fire and Theft Insurance were recommended in most companies with Collision Insurance necessary in about one-half of the companies.

Of the companies owing the cars themselves, all of them paid for and held all insurance policies carried except one. In this case, the company paid the Public Liability, Property Damage, Fire and Theft Insurance, but asked the salesman to pay for Collision Insurance, $50.00 deductible. The reason they gave for asking the salesman to pay the Collision Insurance was that this cost to the salesman would be very small and insurance would cover the car while the salesman was using it for his own pleasure. Six companies that own their own cars carry Collision Insurance on them, and five companies do not carry it. Since Collision Insurance is the most costly type of insurance, companies may be justified in not carrying this type. They could overcome this by teaching their salesmen to drive carefully by giving a small bonus to the men who do not have any accidents in a year, or they could make the salesmen pay for any collision damages themselves.

Of the companies operating salesman-owned cars, ten require the salesman to pay for his own insurance out of the allowance given him for operating his car. Of these ten companies, three require that the salesmen either file their policies with the company, or send copies of them to the company. The reason for this is that the company wants to make sure that their salesmen are properly covered, and to make sure that the company will have no liability in the case of a serious accident. One company takes advantage of the fleet discount for their salesmen by insisting that they take out their insurance through the company. They charge the full amount of this insurance to the salesman, but the cost to him would be less than if he took out the insurance himself, and it gives the company more control at all times, and gives them the assurance that the salesman is properly covered. Three companies either carry a blanket policy covering themselves for contingent liability insurance in case a salesman is in a serious accident, or else insist that a rider be attached to the salesman's policy which will cover the company. In most cases the company insists on Public Liability and

Property Damage and expects the salesman to carry Fire and Theft. Collision Insurance is left entirely to the salesmen in all cases.

The companies with salesman-owned cars help the salesman pay his insurance premium. In both of these cases the insurance is carried through the company itself. One company pays 25% of the premium, the salesman paying the balance, while the other company pays three-quarters of the cost of Public Liability, Property Damage, Fire and Theft. Collision Insurance may be had in the latter case if the salesman wishes it, but it is at his own expense.

Conclusion

It has been found in this survey that quite a number of Canadian companies do not fully appreciate the fact that their salesmen's car expense is a real item in their total expenses. Some of them do not keep accurate records to show the operating expenses in sufficient detail, and it is felt that if they did so they could cut down their expenses considerably. Other companies have very complete records and are getting the maximum efficiency out of the way they are handling their salesmen's cars. Whether it is more economical for the company or the salesmen to own the cars can only be determined by study of the particular situation in the light of all available data. A great many companies might also do well to look into the method they have of paying the salesmen for the use of the car when he owns it.

The problem seems to be identical in all types of businesses and although the majority of the companies referred to in the preceding discussion are manufacturing concerns, it is felt that the results given here should be beneficial to all types of companies operating salesmen's cars in Canada.

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